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REPORT ON REVIEW OF THE INSURANCE REGULATION PROGRAM

February 1974

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REPORT ON REVIEW OF THE INSURANCE REGULATION PROGRAM

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ELECTIVE AND ADMINISTRATIVE OFFICIALS

E. V. "Sonny" Omholt	State Auditor, ex officio Commissioner of Insurance
William E. Smith	Chief Deputy Commissioner of Insurance

SUMMARY OF RECOMMENDATIONS

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Prepare a formal statement of objectives, familiarize all staff members with the objectives, and inform staff members how their work contributes to the objectives.	12
Prepare a plan to assure that objectives are met and revise the plan as necessary to meet changing conditions.	13
Develop and implement an information system that will provide the information needed for management planning and action.	14
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Send applications forms and a complete list of authorization requirements to all companies that request applications.	22
Disapprove, on a timely basis, authorization applications from companies which cannot be authorized.	23
Establish firm written criteria for determining whether insurance companies meet the authorization requirements, apply these criteria on a consistent basis, and document the basis for any exceptions in applying these criteria.	25
Inform unqualified applicants on a timely basis of the reason their applications are not approved.	27

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LICENSING OF INSURANCE AGENTS, SOLICITORS, AND ADJUSTERS

Follow up in those instances where the sponsoring insurance companies don't provide the specified information. 29

Establish written procedures for the licensing of applicants for agent, solicitor, and adjuster licenses. 30

Keep a record of agent, solicitor, and adjuster license applications received and the disposition thereof, including the basis for action taken on each application received. 31

Inform applicants who will not be licensed why their applications were not approved. 32

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SUMMARY OF RECOMMENDATIONS (Continued)

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MORRIS L. BRUSETT, C.P.A.
LEGISLATIVE AUDITOR

G. DEAN REED, C.P.A.
DEPUTY LEGISLATIVE AUDITOR

STATE OF MONTANA
Office of the Legislative Auditor
STATE CAPITOL
HELENA, MONTANA 59601
406/449-3122

The Legislative Audit Committee
of the Montana State Legislature:

We have reviewed the insurance regulatory procedures of the Office of the Montana State Auditor. The following major regulatory functions were included in the review.

Authorization of Insurers

Licensing of Agents, Solicitors, and Adjusters

Examination of Agent and Solicitor Applicants

Approval of Insurance Forms

Review of Annuities

Examination of Insurers

Regulation of Insurers' Security Deposits

Collection and Distribution of Premium Taxes

Action on Insurance Complaints

We did not review numerous other aspects of insurance regulation, such as advertising and trade practices or insurance specialties, such as fraternal organizations, benevolent societies, farm mutual insurers, reciprocal insurers, and others.

The purpose of the review was to determine the extent of compliance with state law, to identify areas where the efficiency and effectiveness of the state insurance regulation program can be improved, and to make constructive recommendations to accomplish the needed improvements. Our audit of the financial transactions of the State Auditor's Office, including the insurance regulation program, was covered in a separate report dated September 21, 1973.

Our audit was conducted in accordance with generally accepted governmental auditing standards and accordingly included such procedures as we considered necessary in the circumstances. We reviewed available pertinent records of the State Auditor's Office; obtained information from insurance commissioners of other states, insurance companies, and insurance agencies; and discussed insurance regulation with departmental officials, insurance agents, and Montana citizens.

We submit the following comments as outlined in the table of contents. In addition, the complete text of the State Auditor's reply is included as the last section of this report.

COMMENTS

SUMMARY

Since Montana began regulating insurance in 1897, the insurance industry has grown significantly and has become far more complex. While many other states have responded to the increasing size and complexity of insurance business by establishing specialized sections for the various types of insurance and by establishing sections for investigations and enforcement, hearings, actuarial rate examinations, and others, the Montana state insurance regulatory function has remained for the most part a clerical operation. The Insurance Department of the State Auditor's Office does not have formal objectives and plans for attaining objectives. The department basically operates on a day-to-day basis without an overall planned approach to fulfill its duties and responsibilities. A more systematic approach to insurance regulation is needed to achieve its mission, and we are making recommendations for increased objective setting and planning.

Departmental Records

The department's records are inadequate or non-existent in several phases of its operations. Because of inadequacies in the records, the department cannot effectively assess its operations and, in some instances, does not have information needed for decision making.

We are recommending improvements in the record keeping and the establishment of a well planned information system.

Authorization of Insurers

The department's procedures for authorizing insurers to do business in Montana are weak in several respects. Systematic application review procedures have not been developed. Applications are not always evaluated on a consistent basis. Applicants whose applications are not approved are not always advised of the reasons for the action.

In order to provide assurance that all authorization applications are evaluated fairly, we are recommending that the department implement systematic application review procedures, implement them on a consistent basis, and advise applicants of actions taken.

Licensing of Agents, Solicitors, and Adjusters

The department has no formal criteria for determining whether license requirements are met and has no formal procedures for evaluating license applications. We found instances where unlicensed persons were acting as agents and adjusters.

To improve the licensing function, we are recommending that the department develop and implement criteria for determining whether license requirements are met and develop written licensing procedures.

Examination of Agents and Solicitors

Numerous weaknesses exist in the department's procedures for examination of applicants for agent and solicitor licenses. Examination grading procedures are ineffective. In some instances, the examiners altered completed answer sheets to provide applicants passing scores.

To correct these weaknesses we are recommending that the department develop and implement examination control procedures and grade all exams fairly and impartially.

Approval of Insurance Forms

The department doesn't have procedures to assure that only approved insurance forms are used in insurance policies sold to the public. We found instances where unapproved forms were used, and there are many complaints from purchasers that the policies they purchased are not what they understood them to be.

To overcome these weaknesses we are recommending that the department develop procedures to assure that only approved forms are used in Montana.

Examination of Insurers

We found several weaknesses in the department's procedures for examination of insurers. The independence of the department's examiners is subject to question based on their current method of compensation. The department's examination procedures and workpapers are inadequate in many respects.

To correct these weaknesses we are recommending improvements in workpaper preparation and examination procedures.

Administration of Security Deposits

The department's administration of security deposits is weak in many respects. The department's procedures for determining whether companies meet the deposit requirements are ineffective and consequently the department has no assurance that all companies have adequate deposits. The department has no procedures for taking action against companies whose deposits are known to be inadequate.

Deposit requirements were established to provide protection to policyholders in the event an insurance company becomes insolvent. Therefore, we are recommending that the department implement procedures to assure that deposits are adequate, and to take corrective action when companies have inadequate deposits.

Premium Taxes

The department has several weaknesses in its procedures for collection and distribution of insurance premium taxes. Among these are that the department's procedures for verifying premium taxes paid are not always effective, which results in companies at times paying incorrect amounts.

Based on current state law, insurance premium taxes are in lieu of other state and local taxes. Therefore, insurance companies may invest in non-insurance operations and pay no tax on any profits earned.

Existing premium tax distribution methods often result in inequitable distributions to local communities.

To alleviate problems related to premium taxes we are recommending that the department clarify premium tax forms, improve tax verification procedures, and consider seeking legislation to tax non-insurance income and resolve the tax distribution inequities.

Insurance Complaints

Numerous weaknesses exist in the department's processing of insurance complaints. We found that many complaints are not investigated adequately and information developed in the complaint section is not fully used to improve the insurance industry in Montana.

To increase the effectiveness of the complaint processing procedures we are recommending more thorough investigation of certain complaints and more effective utilization of information developed by the complaint section.

GENERAL

The State Auditor in Montana is a constitutional official of the Executive Branch of State Government. The State Constitution - both the old Constitution and the recently adopted new Constitution, effective July 1, 1973 - provides that the State Auditor be elected at general elections to serve a four-year term and to perform such duties as prescribed by the State Constitution and law. The old Constitution prescribed no specific duties of the State Auditor. In the new Constitution, the only specific duty designated is that the State Auditor is a member of the State Board of Land Commissioners.

Among the primary duties prescribed by statute, the Office of the State Auditor has been assigned regulation of the insurance industry in the state. Montana began regulating insurance business in 1897 when insurance companies were first required to be licensed and the State Auditor was assigned the responsibility for licensing insurers and administering subsequent regulatory laws. In 1909, the Department of Insurance was created within the State Auditor's Office, and the State Auditor was designated Commissioner of Insurance, ex officio.

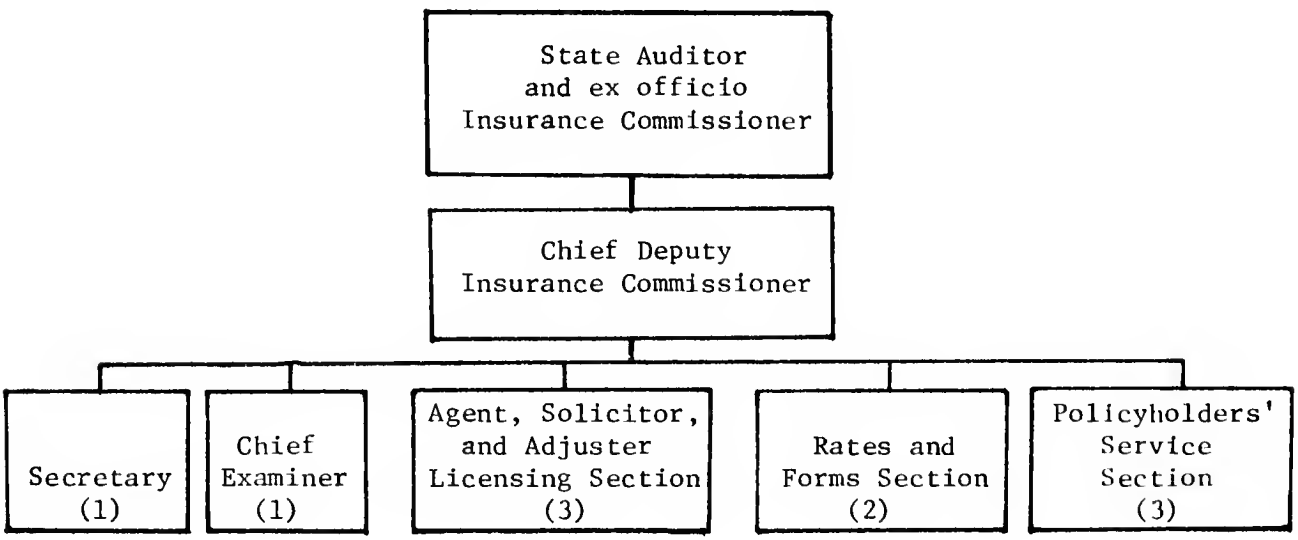
Montana's present laws regulate, to varying degrees, practically all aspects of the state's insurance industry. As in the past, current laws designate the State Auditor as the ex officio Insurance Commissioner. The basic purpose of insurance regulation is to protect the public.

The Executive Reorganization Act of 1971 established standard terminology for the organizational structure of executive branch agencies other than specified elected officials. The State Auditor was one of these officials and accordingly, the organizational structure of his office is not subject to the standard terminology. As a result, the insurance regulatory unit of the State Auditor's Office continues to be known as

the Insurance "Department" and is not one of the 19 "departments" created pursuant to the 1971 reorganization act.

The department's operations are financed from the General Fund and recorded expenditures for 1972-73 were $142,711. As of June 30, 1973, the Insurance Department had a staff of 11. The staff is organized into four sections, each of which is responsible for particular regulatory functions. The department's organization chart and number of employees by section are shown below:

ORGANIZATION CHART
MONTANA INSURANCE DEPARTMENT



Insurance is big business in Montana. Nearly every Montanan is affected by insurance and therefore by insurance regulation. As of December 31, 1972, the department's records show 840 insurance companies were authorized to do business in the state, and about 3,900 agents and solicitors were licensed. The records further show that for 1972, insurers collected $217 million of insurance premiums from Montanans and paid premium taxes of $6,403,417.

In many states insurance regulation is more comprehensive than it is in Montana. Many states have large staffs of specialists for each phase of insurance regulation. Staffs in some states, for example, include economists and financial specialists, financial report analysts, statistical experts, actuaries, attorneys, appraisers, rate examinations staff, investigations and enforcement specialists, hearings officers, administrative and budget specialists, and others. These staff are used to provide intensive regulation of major regulatory aspects, such as licensing insurance companies, rate examination, solvency review, investigation of complaints, and enforcement of insurance laws and regulations.

In addition, many states have extended the insurance regulation to areas not presently encompassed in Montana's Insurance Department. For example, several states:

1. Regulate insurance advertising.
2. Have made extensive studies of insurance rates and, as a result, have required some rates to be decreased.
3. Are studying the language of insurance policies in attempts to develop "plain english" policies that consumers can understand.
4. Have developed rules regulating premium financing.
5. Are studying assigned risk pools for automobile insurance.
6. Regulate cancellation or non-renewal of policies.
7. Have embarked on consumer aid and education programs. One such department has a program to help policyholders understand what they have purchased or are about to purchase. Another such state has issued a handbook to make the public aware of the pitfalls of buying hospital insurance policies through the mail. Another state has launched a massive

consumer education program. As a result of this program, that state's insurance department has issued a series of insurance guidelines including a life insurance shoppers' guide comparing life insurance policies. The guide shows a 300 percent cost variance among policies providing essentially the same coverage. Another of the guidelines provides information and advice on how to select a good insurance agent. Another provides information on how to shop and save on information.

Although the insurance industry has grown significantly in size and complexity, Montana's Insurance Department has remained, for the most part, a clerical operation. The above described activities of other states' insurance departments are areas that should be explored in Montana. To a large extent Montana depends upon other states, the National Association of Insurance Commissioners, and the insurance industry itself to effectively regulate the insurance business and protect the insurance buying public.

As mentioned on page 8, the Montana insurance commissioner has a staff of 11. Most of the staff are paid relatively low salaries and many of the staff had no particular insurance qualifications when they were first employed. As mentioned on page 8, the department's expenditures for 1972-73 were $142,711. A bigger budget will undoubtedly be required if Montana's Insurance Department is to keep pace with the industry and with regulation in other states. Implementation of some recommendations in this report will probably require additional resources to allow the department to acquire staff with technical expertise. Consistent with this need, the National Association of Insurance Commissioners is developing new programs that, if they are to be effectively implemented in Montana, will require more technical expertise.

AGENCY MISSION, ACTION PLAN, AND INFORMATION SYSTEM

AGENCY MISSION, ACTION PLAN, AND INFORMATION SYSTEM

In order to achieve its purposes, every organization, whether public or private, must be aware of its goals, have a plan to achieve its goals, and have an information system that provides relevant information about progress and problems.

Insurance Department's Mission

Every organization must know its purpose. The sole purpose of many small private businesses may be to earn an immediate profit, while larger private businesses may be more interested in long-term gains and may have other purposes. The purposes of governmental organizations generally are more complex and relate to fulfillment of peoples' needs which can't be fulfilled individually or by private business.

The purposes of small organizations often are well understood by everyone in the organization. As organizations become larger and purposes become more varied and complex, the need for formal detailed purpose statements increases. As stated in several sections of Montana's insurance laws and in the State Auditor's annual reports, the purpose of insurance regulation is to protect the public. Insurance and insurance regulation are complex operations which require formal purpose statements. The State Auditor's 1970-71 annual report stated the goal of the insurance program as follows:

> "Provide the individual Montana consumer insurance products with the greatest possible protection while regulating the business in such a way as to encourage the companies to make essential insurance coverage readily available to the public."

The 1971-72 annual report expanded somewhat on the Insurance Department's purposes by adding the following objectives:

1. "Assure the continued solvency of each authorized insurance company to faithfully discharge its obligations to claimants and policyholders."

2. "Ascertain that insurance rates are not excessive, inadequate or unfairly discriminatory."

The 1972-73 annual report did not include the above two objectives.

Other than the annual reports, the Insurance Department has no formal statement of objectives. If the department is to meet its objective of public protection, it should prepare a formal detailed purpose statement. The statement should include the overall public protection goal and compatible objectives for all aspects of insurance regulation. The purpose statement should be distributed to all staff members so they will be aware of objectives and will understand how their work relates to the department's objectives.

RECOMMENDATION

We recommend that the department prepare a formal statement of objectives, familiarize all staff members with the objectives, and inform staff members how their work contributes to the objectives.

Action Plan

Without a plan to achieve its mission, no organization can be assured that it will obtain desired results. The plan must be related to the organization's objectives and must be in sufficient detail to direct all staff members' efforts toward goal achievement.

Plans for mission achievement are often called action plans. Action plans are built upon objectives and lay out, much like a blueprint, the work that must be done to achieve the stated objectives. In addition to stating what is to be done, action plans establish criteria and priorities and may include alternate or contingency plans.

Management without an action plan is frequently called management by crises. Under this system, management and staff actions are directed toward resolving the crisis of the moment. The only assurance provided by this type of management is that there will be another crisis to manage tomorrow.

The department has no action plan. Without an action plan, the department has no assurance that objectives will be met.

RECOMMENDATION

We recommend that the department prepare a plan to assure that objectives are met and revise the plan as necessary to meet changing conditions.

Information System

Every organization needs a management information system that provides timely, relevant information and apprises management what has been done and what remains to be done. Without an adequate information system, management has no way of knowing whether objectives are being met.

An adequate management information system is directly related to objectives and produces information that provides for measurement of objective attainment. For instance, if an objective were to decrease the number of insurance complaints per dollar of insurance sold, the information system would have to record the present complaint level and provide information about the number of complaints and amount of insurance sold.

The department doesn't have a formal management information system. Its 1970-71 annual report listed increased program collections (primarily taxes) and creation of a post assessment guaranty association as its achievements for the year. The report also provided statistical information about the number of agent examinations given, policy forms processed, rate filings processed, and other information. The 1971-72 annual report listed the

collection of a record amount of insurance fees and taxes as a major accomplishment. The 1972-73 annual report was similar to the 1970-71 report in that it reported taxes collected and various statistical information about agent examination and licenses, policy forms, companies authorized, and other information.

Tax collections are pertinent information but aren't related to the department's public protection mission. Statistical information relates more to the mission but can't be related to specific objectives because the department has not prepared a purpose statement or action plan. For example, statistics regarding the number of agents licensed are interesting but lose much of their potential value because no one has determined how many agents there should be or what turnover rate is acceptable for insurance agents.

The department needs an adequate information system to apprise management of results obtained and work remaining to be done. An information system is an integral part of a management system designed to assure mission achievement. Numerous sources of information are available to assist in development of management information systems.

RECOMMENDATION

We recommend that the department develop and implement an information system that will provide the information needed for management planning and action.

AUTHORIZATION OF INSURERS

AUTHORIZATION OF INSURERS

For the public protection, Montana insurance laws (Section 40-2801, R.C.M. 1947) require insurers to be authorized by the department before selling insurance in Montana. Since unauthorized companies cannot do business in the state, authorization is the first step in the insurance regulation process.

The authorization process usually starts with an insurer's request for application forms. Requests are received by the chief examiner who either sends application forms to the company or advises it that it probably doesn't meet Montana requirements. Authorization applications are received and evaluated by the chief examiner and, after consultation with the commissioner and chief deputy, a decision is reached as to whether the company should be licensed. The department issues certificates of authority to authorized insurers.

As of December 31, 1973, 914 companies were authorized to sell insurance in Montana. Of these insurers, 436 were authorized to sell life and disability insurance and annuities, 429 were authorized to sell general property and casualty insurance, and 49 were authorized to sell other types of insurance.

Montana insurance laws establish the following qualifications for insurers seeking to conduct insurance business in this state:

1. Must be incorporated or be a reciprocal insurer.
2. Must not have a name so similar to that of another insurer that it would be likely to mislead the public and must not have a name which tends to deceive or mislead as to the type of organization the insurer is.
3. Must have and maintain minimum unimpaired paid up capital stock (if a stock insurer) or surplus (if a mutual or reciprocal insurer) as shown below.

Kinds of Insurance To Be Sold	Stock, Out of State Mutual and Reciprocal Insurers	Montana Mutual Insurers	Montana Reciprocal Insurers
Life	$100,000	$ 50,000	2/
Disability	100,000	50,000	3/
Life & Disability	150,000		
Property	200,000	100,000	$200,000
Marine 1/	200,000		3/
Casualty			
All types except Workmen's Compensation	200,000	150,000	$200,000
All types including Workmen's Compensation	300,000	200,000	3/
Surety	250,000		3/
Title	100,000		2/
Multiple Lines			
Two or more: property, marine casualty, or surety	400,000		2/

1/ Marine insurance generally means insurance of goods in transit regardless of the transportation mode.

2/ Reciprocal insurers may not write life or title insurance.

3/ Reciprocal insurers may be authorized to write additional kinds of insurance if they have a surplus equal to the minimum capital stock required of a stock insurer for those kinds or combination of insurance.

4. Must have at the time of authorization but need not maintain a surplus:

   a. Insurers with less than five years insurance history must have a special surplus equal to the minimum capital or surplus.

   b. Insurers with more than five years insurance history must have a special surplus equal to 50 percent of the minimum capital or surplus.

c. Insurers transacting multiple lines of insurance must have and maintain a special surplus of $100,000.

5. Must have on deposit with the commissioner cash or securities in an amount at least equal to the minimum required capital except that title insurers need deposit only $50,000 and out of state insurers may make a like deposit with the commissioner of its home state rather than with the Montana commission.
6. Must have principal management personnel who are trustworthy, of good character, competent to manage an insurance business, and are not affiliated with people who have manipulated assets or accounts to the detriment of insurers, stockholders, or creditors.
7. Must apply to the commissioner for a certificate of authority.
8. Must submit the $300 fee for filing application.
9. Must submit various documents including its most recent financial statements and examination (audit) report.

Certificates of authority may be renewed each year by payment of a $300 fee.

Records for Certificates of Authority

The department doesn't keep records of authorization inquiries received, authorization applications received, or the disposition of inquiries and applications. For example, one company, which is not authorized in Montana, advised us it had applied in 1966. The department had no record of the application and the chief examiner said he was not aware of the application. Another company applied in 1966 but was not authorized. It applied again in 1973. When reviewing the 1973 application, the present chief examiner said he was unaware of the previous application because there was no record

of it. He also said he was unaware of the reason(s) the first application was not approved.

A file is maintained for each authorized company. The file includes the application for authorization, a copy of the certificate of authority, the most recent examination report, and other papers and correspondence. There is no record that the company met all the authorization requirements nor is there a record showing how the department staff determined that the company was qualified. For example, the records of one company authorized in October 1970, did not show how the staff determined that the company was qualified. The company's authority was suspended in March 1971, because its capital had been depleted to the point of endangering policyholders.

A sound management system requires adequate records. Without good records, management cannot adequately control operations, cannot determine that desired objectives are being met, and cannot review past actions when need arises.

RECOMMENDATION

We recommend that the department:

1. *Keep a record of authorization inquiries and applications and the status or disposition thereof.*
2. *Develop and use a checklist showing the requirements for the authorization applied for, the staff's determination that the company met or did not meet the requirements, and a reference to the information upon which the determination was based.*

Authorization Fee

Section 40-2726, R.C.M. 1947, provides for a $300 fee ($30 for Montana companies) for filing an application for authorization and issuance of an

original certificate of authority, if issued. The law requires fees to be promptly deposited in the state's General Fund.

Upon receipt of an application, the department's procedure is to deposit the accompanying fee in an uncleared collection account. If the application is approved, the fees are transferred from the uncleared collections account to the General Fund. If the application is not approved, the fees remain in the uncleared collections account unless the insurance company withdraws its application. In the latter case, the fees are refunded.

The chief examiner said fees are initially deposited in the uncleared collections account rather than the General Fund because the department has no authority to make refunds from the General Fund and the department has interpreted Section 40-2726 to mean the fee cannot be collected unless the applicant is authorized. However, Section 79-415, R.C.M. 1947, authorizes state agencies to refund from the General Fund moneys to which the state is not entitled.

As of December 17, 1973, the uncleared collections account included nine $300 authorization fees from companies whose applications ranged from one day old to five years old.

Section 40-2726 provides the fee is for filing an application and issuance of an original certificate of authority, <u>if issued</u>, (underscoring added). This indicates the fee is an application fee as opposed to an authorization fee. However, the commissioner may need to obtain a legal determination to ascertain the status of the fees. In any event, no need exists to deposit fees in the uncleared collections account because refunds can be made directly from the General Fund.

RECOMMENDATION

We recommend that the department:

1. *Deposit all fees received with applications for authorization directly into the General Fund.*
2. *Seek a legal determination as to the nature of these fees and, if necessary, seek legislation that clearly establishes the fee as an application fee.*

Requests for Authorization Applications

Applications for Montana certificates of authority are available only from the department. Therefore, the authorization process starts with a company's request for application forms.

Upon receipt of a request for application forms the chief examiner refers to any available information about the company and decides whether or not to send the application forms. If the forms aren't sent, the chief examiner sends the company a letter stating it is not qualified for authorization in Montana. A letter frequently used for this purpose is the "island hopping" letter.

The island hopping letter states, in effect, that a company cannot be authorized in Montana unless it is authorized in a state contiguous to Montana. A letter to one company that requested application forms stated:

> "On reviewing sources of information available to the Department, it is noted your company is not licensed in States contiguous to the State of Montana, which raises the question as to the reasons why you are leaving the undeveloped territory between the State of domicile and this State. This Department looks with disfavor upon the practice of insurance companies seeking admission into the State of Montana by such 'island hopping' tactics.
>
> "In the event the company has been admitted into the intervening States, then this objection would be removed."

A letter to another company stated the requirement more strongly:

> "We further require that a company be licensed in states contiguous to Montana."

The chief examiner said an insurance company would be unable to adequately service Montana policyholders unless its organization was built on a contiguous pattern rather than an island hopping one. He generally interprets contiguous to mean "close," but has no established criteria for determining whether a company is authorized in a state "close" to Montana. He said the criteria for contiguous to Montana depends on the company's operations, whether a parent or subsidiary company is authorized in Montana, and whether the company has applied to states "contiguous" to Montana.

Island hopping letters are not used on a consistent basis. For example, one company inquired in 1966, 1967, and 1968 about becoming authorized in Montana. Application forms were never sent to the company, and it was advised it couldn't be authorized in Montana because it was not authorized in a contiguous state. In 1966 and 1967, the company was authorized in Kansas and Oklahoma. In 1968, it was authorized in Colorado, Kansas, and Oklahoma. Another company inquired about authorization in Montana, was furnished application forms, applied, and was authorized even though it was authorized only in Kansas, Louisiana, Mississippi, Oklahoma, and Missouri at the time. Apparently, Colorado is not "contiguous." Sometimes Kansas and Oklahoma are "contiguous" and other times they aren't.

The chief examiner said island hopping letters are sometimes used when the department prefers not to authorize a company even though it meets the statutory requirements. For example, a company may meet the statutory capital requirements but may, in the department's opinion, be undercapitalized. The chief examiner said the island hopping letter is at least 40 years old and still works, so why change.

Montana laws do not require a company to be authorized in a contiguous state before being authorized in Montana, and the department has not issued a regulation requiring contiguous authorization. The department should discontinue using such methods as island hopping letters to preclude insurance companies from being considered for authorization. All companies should be treated equitably and application forms should be sent to all companies requesting them.

RECOMMENDATION

We recommend that the department:

1. *Establish in writing and publish, insofar as practical, authorization requirements which are in addition to statutory requirements.*
2. *Send application forms and a complete list of authorization requirements to all companies that request applications.*

Rejection of Applications for Authorization

Section 40-2812, R.C.M. 1947, requires the department to act upon authorization applications within 30 days after their completion, authorize qualified companies, and to refuse authorization of unqualified companies.

The department does not reject applications from companies which will not be authorized. The chief examiner said rejection of an authorization application would tarnish a company's record and make it difficult for it to be authorized in other states. The department either returns applications without formally rejecting them, suggests that applications be withdrawn, or simply does not take final action on applications from companies which will not be authorized.

The department may hold, for long periods, applications which it has no basis for returning or suggesting withdrawal. For example, in October 1973, the department had on file a 1969 application from one company. No actions had been taken on the application since September 1969. As a result of our inquiry as to the status of this application, the company withdrew its application and the department refunded the $300 fee. Another application on file in the department was dated August 1969, and the department had taken no action since October 1969. The company informed us it no longer had a record of the application because it was so old. The department was still holding the company's $300 fee.

Insurance departments of several other states, including Wyoming, Idaho, Florida, Utah, South Dakota, and New York, informed us they do not hold applications which will not be approved. Applications which cannot be approved are disapproved.

RECOMMENDATION

We recommend that the department disapprove, on a timely basis, authorization applications from companies which cannot be authorized.

Enforcement of Authorization Requirements

The department does not always apply authorization requirements on a consistent basis. For example, as discussed on page 21, the department's requirement for authorization in contiguous states is not applied consistently. Also, the requirement that companies submit a current examination report with their application is not consistently enforced.

Section 40-2713, R.C.M. 1947, requires the department to examine the operations and financial condition of each insurer applying for initial authorization in Montana. In lieu of making its own examination, the

department may accept the full report of the last recent examination of an out-of-state company if the report is certified by the insurance supervisor of that state. Section 40-2811, R.C.M. 1947, requires insurers to submit copies of their last examination report with their applications for authorization.

The department has no established criteria as to what constitutes a recent examination other than it "is contingent on the company's size-financial-age-reputation." However, three years is often considered the rule because the insurance laws require the department to examine Montana companies at least once every three years.

One company which applied in 1969, but has not been authorized, was advised it could not be authorized at that time because its examination report was over three years old. The department's letter stated:

> "The Montana Insurance Department will, also, require a more recent examination report. Section 40-2713, R.C.M., provides that the commissioner may accept a report certified by the supervisory official of another state. However, this report must be current within the 3 year period."

Other companies were authorized even though their most recent examination reports were over three years old. For example, one company applied in November 1972, and was licensed in February 1973. The last examination report for the company was more than four years old.

The chief examiner said in some instances companies are authorized with an examination report over three years old because some states examine their insurers on four or five year intervals. In other cases the report may be over three years old before the examining state issues the report. Therefore, many times it is not possible for the insurer to provide a report that is current within the three-year period. Apparently "recent" examination reports are required only if some other state has examined the company "recently."

If examination reports are to serve a useful purpose in the authorization process, they must be current. If other states cannot furnish recent examination reports, the department should have the companies examined.

All authorization applications should be considered based on established criteria and the basis for any exceptions to this policy should be documented.

RECOMMENDATION

We recommend that the department establish firm written criteria for determining whether insurance companies meet the authorization requirements, apply the criteria on a consistent basis, and document the basis for any exceptions in applying these criteria.

Notification to Applicants Whose Applications Are Not Approved

The department does not always inform a company of the reason its application has not been approved. We noted a number of such instances. For example, one company first applied in 1966 and was not informed of the status of its application or why the application had not been approved. Following is a brief chronology of events regarding the application.

November 18, 1965 - Company requested application forms.

November 23, 1965 - Insurance Department sent island hopping letter.

December 1, 1965 - Company responded that it had recently been authorized in Colorado, had an application pending in Wyoming, and intended to apply in North Dakota, South Dakota and Idaho.

December 13, 1965 - Insurance Department sent application forms and suggested the company withhold its application until its 1965 financial statements were completed.

April 6, 1966 - Company applied. Application included 1965 financial statements, other documents, and the $300 fee.

May 10, 1966 - Insurance Department returned one of the necessary forms because the company's corporate seal was not affixed to it. (Note: There is no statutory requirement that the corporate seal be affixed.)

May 13, 1966 - Company resubmitted the form with its corporate seal affixed.

September 6, 1966 - Company inquired about the status of its application and offered to furnish any additional information needed.

January 5, 1967 - Company inquired about the status of its application.

February 14, 1967 - Company inquired about the status of its application and submitted 1966 financial statements.

May 11, 1967 - Company inquired about the status of its application.

May 18, 1967 - Insurance Department responded to the company's inquiries. A letter advised the company its filings were complete and up-to-date. The letter continued: "However, we have approximately thirty-five companies wanting to be admitted in Montana. This not only takes time, but our Chief Deputy had to take an emergency leave and will be gone at least three weeks and he and Mr. Omholt have the final say on all new companies desiring admittance. If they have any questions concerning your application, you will be notified."

December 1967 - The Insurance Department returned the company's $300 check as a result of an audit recommendation that checks held by the state auditor be deposited or returned.

In May 1973, the company engaged an attorney to submit a new application on its behalf. The application is still pending because the department requested a more recent examination report from the company. The examination report submitted with the application was for the three years ending December 31, 1969.

The company informed us the department had never advised it that it did not qualify for authorization in Montana. The company further stated

". . . it does seem unreasonable that after eight years we appear to be no nearer to admission than we were when we started."

Standard operating procedures should be developed to keep applicants advised of the status of their applications and to inform unqualified applicants of the reasons their applications are not approved. The department should respond promptly to inquiries as to the status of an application.

RECOMMENDATION

We recommend that the department inform unqualified applicants on a timely basis of the reason their applications are not approved.

LICENSING OF INSURANCE AGENTS, SOLICITORS, AND ADJUSTERS

LICENSING OF INSURANCE AGENTS, SOLICITORS, AND ADJUSTERS

Section 40-3307, R.C.M. 1947, provides that no one in the state shall act as or hold himself out to be an insurance agent or solicitor unless licensed to do so. Generally, an agent represents an insurance company and, if authorized by the company, may contract for it. A solicitor represents an agent and may solicit insurance applications for such agent but may not contract. An adjuster investigates and negotiates settlement of claims arising under insurance contracts. Agents and solicitors must be licensed for each type of insurance they sell or solicit, but solicitors may not solicit applications for life or disability insurance. Licensed adjusters may adjust losses for all types of insurance.

The insurance laws require the department to determine whether applicants are qualified for the licenses applied for and that only qualified applicants may be licensed. Applications for new agent, solicitor, and adjuster licenses are reviewed by the department's licensing section, which is staffed by a supervisor and a clerk.

The department has no readily available record of the total number of licensed agents, solicitors, and adjusters, but estimates that about 20,000 licenses and renewals were issued during 1972-73. This does not reflect the number of people licensed because many people are licensed with more than one company. We estimate that about 3,900 people are licensed as agent or solicitor, and about 100 people are licensed as adjusters.

Criteria For Determining That License Requirements Are Met

The insurance regulatory laws prohibit the licensing of agents and solicitors who fail to meet certain criteria specified in the law. For example, the law requires applicants to be competent, trustworthy, of good

reputation, and have had experience and training, or otherwise be qualified for the license he seeks. The licensing section relies on insurance companies to screen their agents. Included on the application forms is space for the appointing insurance company to certify that the applicant -

(1) is trustworthy, and

(2) is qualified to act as an agent for the company.

On 19 percent of the applications we reviewed, the insurance companies didn't check these boxes. The licensing supervisor said they usually license applicants without determining why these boxes aren't checked, as long as the company signs the application.

The department has no written criteria of its own to determine if applicants meet these basic requirements. Since the department relies upon the sponsoring insurance companies to determine the applicants are trustworthy and qualified, it should follow up in those instances where the companies do not complete the applications to verify the omissions are nothing more than oversight.

RECOMMENDATION

We recommend that the department follow up in those instances where the sponsoring insurance companies don't provide the specified information.

Licensing Procedures

The licensing supervisor stated there are no written procedures for licensing agent, solicitor, and adjuster applicants. She said the licensing requirements and procedures just had to be learned through experience. The licensing clerk said she had about 10 years' experience and still didn't know all the requirements and procedures.

Written procedures are necessary to provide guidance for the licensing staff to assure themselves that all licensing requirements are met and to provide for continuity of the licensing function during times of employee turnover. Such procedures should include a statement of all licensing requirements and such processing steps as necessary to assure the licensing staff that each applicant meets all requirements. For example, if the licensing clerk and licensing supervisor simultaneously terminated their employment with the department, the replacement staff would have to start from "zero" in learning the licensing requirements and procedures. Such a situation would probably result in a temporarily ineffective licensing function.

RECOMMENDATION

We recommend that the department establish written procedures for the licensing of applicants for agent, solicitor, and adjuster licenses.

Records of Applications

The licensing section doesn't keep records of applications received and the disposition thereof. There is no record of applications received but not approved, and there is no record showing that applicants approved for licensing met all the license requirements.

A file folder is prepared for each person whose application is approved. The application, appointment from an insurance company, and all other subsequent information is kept in the folder.

A sound management system requires adequate records. Such records would enable a more timely review and provide a data base for analysis to aid in determining if desired objectives are being met.

RECOMMENDATION

We recommend that the department keep a record of agent, solicitor, and adjuster license applications received and the disposition thereof, including the basis for action taken on each application received.

Applications Not Rejected

The licensing supervisor stated that very few, if any, applications are actually rejected. If there is some reason why immediate action cannot be taken or the licensing staff believes an applicant should not be licensed, they advise the insurance company that appointed the individual and the company usually withdraws the request for licensing. Upon receipt of the company's request to withdraw the application, the licensing staff returns the application, licensing fees, and all related papers. No record is kept of the individual's application nor does the department inform the applicant of the reason his application was not approved. If the individual should, at some future date, apply for a license to represent the same or another company, the licensing staff would have no record of the previous application or of the reason for not licensing the applicant. Any new employees would be unaware of all such previous actions.

Section 40-3315(1), R.C.M. 1947, requires the department to promptly issue licenses to qualified applicants and, by implication, also gives to the department the responsibility of rejecting unqualified applicants and informing them why their applications are rejected.

Several other states, including Idaho, Wyoming, North Dakota, South Dakota, New York, Florida, and Utah informed us they inform applicants of application disapproval and explain the reasons for disapproval.

RECOMMENDATION

We recommend that the department inform applicants who will not be licensed why their applications were not approved.

Unlicensed Agents

Section 40-3307, R.C.M. 1947, states that no person shall act as or hold himself out to be an agent or solicitor in this state, unless then licensed as such agent or solicitor. The law further provides no agent or solicitor shall solicit, take application for, procure, or place for others any kind of insurance as to which he is not then licensed.

Unlicensed agents are taking applications for and issuing policies of personal travel accident insurance at airports in Montana. Three unlicensed agents sell insurance at one major airport in Montana, three unlicensed agents sell insurance at another such airport, and four unlicensed agents sell insurance at still another such airport. Other unlicensed agents may sell insurance at other locations. The policies sold by these agents are a limited type of life and disability insurance which provides coverage only during specified trips on commercial transportation systems. This insurance is commonly called trip insurance.

The unlicensed agents at two of the airports were employed by a licensed agent but were not always supervised by him. The unlicensed agents at the other airport were employed by the operator of a car rental business. The car rental operator was not an insurance agent. A former clerk of the car rental business was a licensed trip insurance agent but is no longer employed at the car rental business. One of the present unlicensed agents at this location informed us she was planning on obtaining a trip insurance agent's license. At the time of our review, policies were being sold under the former employee's name.

The chief deputy said that he was not sure whether these people should be licensed. He referred to Section 40-2822, R.C.M. 1947, which states that an agent may, by express written authorization given in advance, delegate to his salaried clerical employee the power to countersign the name of the agent on such contracts or classes of contracts as are designated in such authorization. This may be done so long as the initials of such employees are written below the agent's name on such countersignature, but the agent shall not thereby delegate the authority to bind an insurer to a risk not already bound by the agent. The unlicensed agents at the three airports are binding new risks.

Trip insurance is a form of life and disability insurance and Section 40-2822 specifically states that it does not apply to life and disability insurance. Nothing in the codes permits life insurance agents to delegate their duties. As was discussed on page 32, Section 40-3307, R.C.M. 1947, prohibits unlicensed persons from soliciting, procuring, or placing for others any kind of insurance for which he is not then licensed.

Because of the limited nature of this insurance, it may be advisable to exclude trip insurance from licensing requirements.

RECOMMENDATION

We recommend that the department determine the necessity of licensing agents and solicitors for trip insurance and either implement procedures to assure that they are licensed or propose legislation to exclude this type of insurance from the requirement for licenses.

Insurance Vending Machines

Section 40-3322, R.C.M. 1947, permits licensed resident agents to issue personal travel accident insurance policies by mechanical vending machines supervised by the agents and placed at airports and similar places where transportation tickets are sold, provided that:

-- The policy to be sold provides reasonable coverage and benefits.

-- The vending machine used is reasonably suited for the purpose.

-- Reasonable means are provided for informing prospective purchasers of the coverage and restrictions of the policy.

-- Reasonable means are provided for refunding money inserted in defective machines.

Vending machine licensing is done by the department's licensing section. As of September 1973, insurance vending machines were licensed at four of the larger airports in Montana.

We reviewed policies from the vending machines at three of these locations. The agent who countersigned the policies was not the same agent who had obtained a license to sell policies from these machines. The agent who countersigned the policies said the insurance company had requested him to become the agent of record on the policies issued from the machines and he agreed to do so. The agent stated that, except for the use of his name on the policies, he had nothing to do with the vending machines. He doesn't service the machines, as required by law.

The agent who had obtained licenses to sell policies from the machines was unaware that another agent was selling policies from the vending machines. Also, he didn't know the location of the vending machines or

who serviced them. He said he was merely the agent of record for the vending machines and had no real involvement with them. He received a fee from the insurance company for being the agent of record.

The insurance company that writes the vended policies advised us it had changed the agent of record and was unaware that the former agent of record had the present license to sell policies from the vending machines. Subsequently, the company informed the department that they would have the machines licensed for the new agent. However, the machines had not been relicensed as of December 5, 1973.

Each vending machine must be licensed and must display proof of the existence of such license. The department is required to revoke the license issued for any vending machine that ceases to meet the statutory requirements (Section 40-3322, R.C.M. 1947).

The department does not inspect insurance vending machines prior to their licensing nor does it periodically inspect licensed machines. We examined the flight insurance vending machines at two major airports. One machine complied with the requirements of Section 40-3322, except that the 1972 license was displayed rather than the 1973 license. The other machine displayed neither a license nor a serial number.

In addition to the problems with the licensed machines, an unlicensed machine is located at another major Montana airport. Additional unlicensed machines may be located at other airports, depots, and railroad stations throughout the state. The unlicensed machine we observed does not meet the statutory requirements for insurance vending machines. The machine doesn't provide a reasonable means for refund to the applicant for loss of money due to defect in the machine, nor does it inform a prospective purchaser of restrictions of the policy.

RECOMMENDATION

We recommend that the department implement procedures to effectively control the sale of insurance policies through vending machines.

Unlicensed Independent Adjusters

Section 40-3306, R.C.M. 1947, states that persons who adjust losses for only one insurance company or for only one insurance agent shall not be defined as adjusters. The department has interpreted this section to mean that adjusters working for only one company or one agent need not be licensed.

Questionnaires we sent to a limited number of insurance agencies throughout the state showed that at least three unlicensed adjusters were working for a large adjusting organization in the state. Upon being advised of these unlicensed adjusters, the company's regional manager said they were trainees and he was not aware that trainees had to be licensed. He told the department staff that he would send license applications in for these three adjusters immediately. One of these "trainees" advised us he was the only adjuster in one of the company's branch offices, and that he adjusted all types of losses.

RECOMMENDATION

We recommend that the department periodically notify adjusting companies of the need for all independent adjusters to be licensed and develop and implement a system to determine if unlicensed adjusters are adjusting losses in Montana.

Examination Requirements

Insurance agent and solicitor applicants must be examined before being licensed. Presently no examination is required to be licensed as an

adjuster in Montana. Applicants for adjusters' licenses in Idaho, Oregon, Utah, New York, and others must pass an examination. Of the Montana insurance agents who responded to the question on our questionnaire, nearly one-half said they believed adjusters should be examined. One agent who said adjusters should be examined explained that adjusters have more effect on payments under policyholders' claims than agents do. Another agent explained that adjusters have a big responsibility and need to be knowledgeable. Agents who said adjusters need not be examined generally explained that most adjusters are competent because they receive company training or said there is already too much government regulation.

Examination of adjusters is especially important since the department has no other means of determining adjuster applicants' competency.

RECOMMENDATION

We recommend that the department determine the feasibility of requiring applicants for adjuster licenses to pass a written examination.

Flag Files

The department maintains a file, called the "flag file," listing people who have violated insurance codes of Montana or other states, or have had devious dealings in insurance, or whose backgrounds may preclude them from being licensed as agents or solicitors. The licensing section uses the flag file to preclude the licensing of unscrupulous persons.

The licensing supervisor said applications for agent and solicitor licenses are screened against the flag files, and applications from people listed in the flag file are referred to the chief deputy. The chief deputy said people whose names are in the flag file and who have serious charges against them are not licensed. Those with no serious charges against them

are asked to come to the department's offices for an interview, and the chief deputy decides whether or not to license them based on the interview.

Records for Persons Listed in the Flag File

Records for persons listed in the flag file consist of information obtained when, and if, (1) the individual was previously licensed, (2) termination reports were submitted by insurance companies for any previously licensed person, and (3) any memorandums of legal action or any other papers pertaining to a listed person were received. Generally, the word "flagged" will be written on a document in a person's file, on a separate sheet of paper, or on a card. Sometimes the "flag" notation will be accompanied by a date and the initials of the person making the note.

The flag files normally do not state why the individual has been listed in the file, and in many instances the flag notation was not dated, signed, or initialed. We asked the chief deputy why five persons were listed in the flag file. He said he did not know why four of these individuals were listed as flagged and, in some cases, he didn't know when they had been listed or who had listed the individual in the flag file.

Some individuals had been "flagged," "unflagged," then "flagged" again. For example, one person was "flagged" in May 1967, the "flag" was removed in November 1968, and he was "flagged" again in February 1970.

The individual was terminated by one company in May 1967. The company's termination report disclosed that the agent had withheld premiums, but the facts surrounding termination of employment were listed as "decided to work for another company." The termination report was marked "flagged." A later memo in the file stated the person could be licensed and in November 1968, he was again licensed by the company that had previously terminated him. The company terminated him for lack of production in May 1969. He was

then employed by another company but was terminated in October 1969, because he had resigned. The person is presently listed in the flag file.

The chief deputy said he thought the individual was "flagged" for misrepresenting securities; however, the records contain no information regarding misrepresentation of securities and do not show why the person was licensed the second time or why he currently is "flagged."

Some individuals were "flagged" for one kind of insurance but not for other kinds of insurance, and some were "flagged" for insurance purposes but not for security salesman purposes. For example, the file for one individual stated "Flagged May 31, 1967," and a subsequent memo stated "Flag removed for life insurance, May 15, 1968." A third entry showed "To remain flagged for other licenses." Apparently this individual was originally flagged for withholding premiums; however, the records did not show why his "flag" had been removed for life insurance. The chief deputy said he was unaware of the reasons for this action.

To be a useful management tool, the flag file should show the date and reason each person was listed in the file and the dates and reasons for all subsequent actions. Without this information, managers are not in a position to make informed decisions and there is no basis for continuity during periods of personnel changes.

RECOMMENDATION

We recommend that the department keep adequate records of the date of each action in the flag file and of the reasons for flagging a person and for removing the flag for any person.

Criteria for Listing People in the Flag File

There are no written criteria for listing a person in the flag file or for licensing a person listed in the file. Decisions to list a person

in the flag file or to remove a person's "flag" are based on whatever information is available at the time. As discussed above, the flag files do not show reasons the people were flagged, nor do they show reasons the flags were removed.

Without sound criteria as to when a person should be listed in the flag file or when a person's "flag" should be removed, there is no assurance that the file protects the public against unscrupulous insurance agents or that all applicants for agent or solicitor licenses are treated equitably by the state.

RECOMMENDATION

We recommend that the department develop written criteria for listing people in the flag file, for removing flags, and for licensing people listed in the flag file.

Licensing of Persons Listed in the Flag File

In some instances a person listed in the flag file may be licensed. For example, the chief deputy may decide, based on a personal interview, that a "flagged" person may be licensed. These actions are not documented in the file and, in many cases, there is no evidence to show the individual appeared for an interview, the results of any such interview, and the reasons for licensing or not licensing the individual.

For example, one individual was flagged on May 31, 1971, apparently because he had, as a licensed agent, withheld an insurance application and premium. His license was terminated on May 31, 1971. The individual applied for a new agent's license on June 8, 1972, and was licensed that same day. There is no indication in his file showing whether the licensing staff had screened his application against the flag file, whether he was

interviewed by the chief deputy, the results of any such interview, or the reason the individual was licensed. On September 5, 1972, the individual's second license was terminated because he collected a premium but did not turn it in. The individual was flagged again on September 12, 1972. The chief deputy said he didn't know why the individual had been licensed the second time.

If the flag file is to fulfill its objective of protecting the public, applications for agent or solicitor licenses should be screened against the flag file and unscrupulous persons should not be licensed.

RECOMMENDATION

We recommend that the department:

1. *Develop and implement a system to screen all applications for agent and solicitor licenses against the flag file.*
2. *Document all reasons for licensing individuals whose names have been flagged.*

EXAMINATION OF AGENT AND SOLICITOR APPLICANTS

EXAMINATION OF AGENT AND SOLICITOR APPLICANTS

Section 40-3313, R.C.M. 1947, requires the department to test in writing the competence of each applicant, with certain exceptions mentioned below, for an agent or solicitor license. Examinations for agents must cover all the types of insurance for which the applicant has applied to be licensed, as follows:

-- Life insurance
-- Disability insurance
-- Property insurance
-- Casualty insurance
-- Vehicle insurance
-- Surety insurance

Applicants for solicitor licenses must be examined in each kind of insurance, except life, for which their appointing agent is licensed.

Applicants who need not be examined are those who (1) may be licensed under the grandfather clause, (2) are applying for a nonresident license and live in a state that has a reciprocity agreement with Montana, or (3) are applying for a license to sell title insurance or certain other specialty types of insurance.

Agent and solicitor examinations are given by one of three investigator-examiners in the department's policyholders' service section. The examiners grade the tests and inform the licensing section of each applicant's score. The passing score is 70 percent.

During 1973, 985 examinations were given.

Periodic Revisions of Examinations

The examinations were prepared in 1961 as a result of the law requiring examination. The exams have never been revised. One examiner said they

possibly include a few outdated questions but not enough to cause any harm.

Many states revise their examinations periodically. For example, Oregon revises exams every six months, and South Dakota revises exams every two years. The New York Insurance Department informed us that it creates new tests for each examination.

If examinations are to adequately test the insurance knowledge of applicants for agent or solicitor licenses, the examinations should be periodically revised to reflect changing conditions in the insurance industry. Periodic revisions would also reduce the possibility of the exam becoming available to examinees in advance. The chief deputy said the department is now preparing new exams.

RECOMMENDATION

We recommend that the department revise the agent and solicitor examinations periodically and, at the time of each revision, establish a date for the next revision.

Number of Versions of Each Examination

The department has only one version of the examination for each type of insurance. Applicants who fail an examination and are later reexamined retake the same examination. The process can be repeated until applicants pass the exam, from memorization if nothing else. For example, one applicant failed the life and disability exam four times during a six-week period in 1973, and then passed the test on his fifth try.

Several states use multiple versions of each exam. For example, Wyoming and Idaho use two versions of each agent and solicitor exam, and Florida uses five versions of each exam.

Multiple versions of each exam would more adequately test the insurance knowledge of applicants who initially fail the test.

RECOMMENDATION

We recommend that the department prepare and use multiple versions of each examination.

Control Over Examination Booklets

The examination booklets were printed in 1961 and the examiners said no additional copies had been printed since then. The exams are stored in two locations. Exams which have been bound with covers are stored in the State Auditor's Office and locked up at night, and those which have not been bound are stored in the office's basement storage area. The bound exams are used to test applicants for agent and solicitor licenses. The unbound exams are extra copies which are bound for use as needed.

There is no record of the number of exams printed in 1961, and the examiners didn't know whether the exams stored in the two above mentioned areas are all that were printed or if others exist in unknown areas. The exams were serially numbered when printed, but the serial numbers have not been used to effectively control the documents.

The exams to be bound with covers were not always taken in sequential order from the unbound exams in the storeroom. For example, life and disability exams No. 61 to 86 are bound for testing use. Exams No. 87 and 89 were unbound and located in the storeroom, exams No. 88 and 90 to 100 were bound for testing use. Exam No. 64 was unaccounted for.

There are no procedures for taking periodic inventories of the examination booklets. The only inventory taken was in 1970, and it was not accurate because we found 24 examination booklets which were not listed

in the 1970 inventory. The 1970 inventory disclosed at least 37 examination booklets were missing; however, no control procedures were implemented as a result of the inventory, and no inventories were taken subsequently. By August 1973, 12 examinations listed in the 1970 inventory were unaccounted for.

Since there is no record of the number of exams printed, there is no way to tell how many are missing. However, our inventory disclosed that at least 40 examinations were unaccounted for based on the assumption that an exam was printed for each serial number used. Because the exams were not used in sequential order, it is impossible to determine whether the missing exams were among those used for examinations, or those stored in the storeroom.

The examinations are the department's only means of determining the insurance knowledge of applicants for agent and solicitor licenses. Therefore, it is important that the examination booklets be controlled within the department. This is especially important in view of the fact that exams are not revised periodically.

RECOMMENDATION

We recommend that the department take an immediate physical inventory of all examination booklets, establish an accountability record for the booklets, post the record for additional exams printed and the disposition of all booklets, use exams in sequential order, and take periodic inventories in the future and reconcile with the record.

Number of Questions on Each Type of Insurance Exam

The number of examination questions for each type of insurance is as follows:

Type of Question	Number of Questions
General (Insurance Codes)	50
Life Insurance	50
Disability Insurance	50
Property Insurance	25
Casualty Insurance	25
Vehicle Insurance	25
Surety	20

The questions were compiled into the following different exams needed to test applicants for the various types of insurance license for which they apply.

Exam	Number of Questions of Each Type	Total Questions
Life	50 General, 50 Life	100
Disability	50 General, 50 Disability	100
Life and Disability	34 General, 33 Life, 33 Disability	100
Property	50 General, 25 Property	75
Casualty	50 General, 25 Casualty	75
Vehicle	50 General, 25 Vehicle	75
Surety	50 General, 20 Surety	70
Multi-Line	50 General, 20 Property, 10 Casualty, 15 Vehicle, 5 Surety	100

Under this arrangement, an applicant for several types of insurance licenses will be tested on fewer questions for each type insurance than will an applicant for only one type of license. For example, an applicant for property, casualty, vehicle, and surety insurance licenses will have only five exam questions on surety, while an applicant for a surety only

license will have 20 exam questions on surety. The examiners said they varied the number of questions on each type of insurance in order to have a total of 100 questions whenever possible.

If insurance examinations are to protect the public by allowing only knowledgeable applicants to be licensed, applicants for agent or solicitor licenses should be thoroughly examined for each type insurance they will be licensed to sell.

RECOMMENDATION

We recommend that the department test each applicant on all of the questions for each type of insurance he is to be licensed for.

Examinations For Disability Insurance

Section 40-3313, R.C.M. 1947, requires applicants for agent licenses to be examined for each type of insurance for which they will be licensed. The department presently licenses agents for disability (accident and health) insurance if they:

-- Pass the disability insurance exam, or

-- Pass the life and disability insurance exam, or

-- Pass the multi-line insurance exam.

The multi-line exam does not include an examination for disability insurance.

As of December 1973, about 1,750 agents were licensed to sell disability insurance as a result of passing the multi-line exam. The chief deputy said casualty and vehicle insurance often include insurance for medical expenses. He said this medical coverage actually constitutes disability insurance and therefore he believed the agents and solicitors dealing in this type insurance should be licensed for disability. However, individuals licensed for multi-line and disability are licensed to deal in all types of

disability insurance, not just medical insurance included in casualty or vehicle insurance.

Occasionally other states request information about agents licensed or formerly licensed in Montana when they apply for a license in the new state. Any state requesting information about Montana agents licensed for multi-line and disability normally receives the following information:

-- Agent is, or was, licensed for property, casualty, vehicle, surety, and disability.

-- Agent qualified by examination.

The other state may then license the individual for disability insurance based on the belief that the person had been examined for disability insurance in Montana, when he may not have been.

Over 50 percent of insurance complaints received by the department involve disability (accident and health) insurance. This indicates a need for disability agents to be knowledgeable of, and to be examined for, disability insurance.

RECOMMENDATION

We recommend that the department require all agents licensed for disability insurance to pass the disability examination.

Examination Graded as a Whole

Examinations are graded as a whole rather than separately for each type of insurance for which the applicant is to be licensed. The passing examination score is 70 percent overall for all types of questions.

Under this system, an applicant taking the multi-line examination could miss all 10 of the casualty questions, all 15 of the vehicle questions, and all five surety questions and still be licensed for property insurance, casualty insurance, vehicle insurance, and surety if he correctly answered

the 50 general (insurance code) questions and the 20 property insurance questions.

Fifty percent of agents and solicitors in a sample of those licensed in 1972 scored less than 70 percent on one or more types of insurance questions. Some examples are listed below:

	Examination Taken	Overall Score	Score (Percent) On Individual Types of Insurance Questions					
			General	Life	Property	Casualty	Vehicle	Surety
Agent A	Multi-Line	86	92		80	90	67	100
Agent B	Multi-Line	80	78		85	90	87	40
Agent C	Life	75	84	66				
Solicitor A	Multi-Line	70	80		65	80	40	60
Solicitor B	Multi-Line	78	84		80	80	60	60

In our sample, six percent of the multi-line applicants scored lower than 70 percent on the property portion of the exam, 44 percent scored lower than 70 percent on the vehicle portion, and 38 percent scored lower than 70 percent on the surety portion. However, these applicants were licensed for property, casualty, vehicle, and surety insurance because their overall examination score was higher than 70 percent.

Questionnaires we sent to insurance commissioners of other states indicated that applicants for agent or solicitor licenses in several states, including Idaho, North Dakota, and Oregon are graded separately for the various types of insurance and are licensed only for those types for which they obtain a passing score.

To make the exams more effective tools for protecting the public, the separate sections should be graded separately, and applicants for agent or solicitor licenses should be licensed only for those types of insurance for which they obtain a passing score.

RECOMMENDATION

We recommend that the department grade each type of insurance questions separately and license applicants for only those types of insurance in which they scored 70 percent or higher.

Examination Grading

The insurance examinations are multiple choice type tests. Applicants complete the tests by marking their answers on an asnwer sheet provided by the department. The answer sheets are marked by blackening in the space between parenthesis signs for the answer the applicant selects. If the applicant selects multiple choice answer "C" as the correct answer to a question, he marks his examination answer sheet as shown below:

(A) (B) (●) (D)

To grade the exams, the examiner places a cardboard template over the completed answer sheet. If the applicant's black mark (●) shows through the template, the question is graded as correct. If no mark shows, the examiner places a red felt tip pen through the template and makes a red dot on the answer sheet. After grading the entire test, the examiner removes the template and counts the number of red dots. The exam score is determined by subtracting the number of red dots from 100 or, if there were less than 100 questions on the exam, by calculating the percentage of correct answers.

Numerous examinations were incorrectly graded. Incorrect grading was the difference between passing and failing for those who scored near 70 percent. In 1972, 63 percent of those who were given a score of 70 and were licensed as agents or solicitors actually scored less than 70 and should not have been licensed. The examiners stated that prior to January 1973, examinations were graded at the examination site. They said the

incorrect grading probably was the result of nervousness caused by applicants standing over them watching them grade the exams. Starting in January 1973, the examiners have been grading the exams in their office and said this procedure should resolve any problems with incorrect grading.

We reviewed all of the exams which received a score of 70 percent from January 1, 1973, to June 30, 1973, and found that 50 percent were incorrectly graded. There were four causes, as listed below, for incorrect grading.

Cause for Incorrect Grading	Percent of Exams Incorrectly Graded for This Cause	
	1972(1)	First 6 Months of 1973
1. Answer sheets were altered.	29	19
2. Incorrect answers were not marked wrong.	32	25
3. The number of wrong answers was counted incorrectly.	6	6
4. The percentage score was calculated incorrectly.	3	0

(1) Percentages add to more than 63 percent because some exams had more than one type of incorrect grading.

In addition to the incorrectly graded exams, the examiners could not explain how they graded one exam. Each type of incorrect grading and the unexplained exam are discussed below.

Alteration of Answer Sheets

Section 40-3314(4), R.C.M. 1947, requires the department to give, conduct, and grade all examinations in a fair and impartial manner and without unfair discrimination between individuals examined. However, the examiners altered many examination answer sheets to provide the applicants passing scores. The alterations were done after the exams were graded by blackening over one or more red dots.

The examiners gave us varying explanations for the alteration of examinations, some of which confirm their knowledge of the discrepancies. In summary, there has been a general lack of concern on the part of some of the examiners in grading exams.

The chief deputy said the examiners either individually or collectively apparently had the idea it was all right to pass applicants as long as they got "close" to 70 percent on the exam. He said he had no knowledge of how the staff got that idea and said that if the exams were being altered, it was being done without management direction.

Wrong Answers Not Marked Wrong

On many examination answer sheets wrong answers were not marked wrong, i.e., no red dots were placed on the answer sheet for one or more questions which were incorrectly answered. This type of incorrect grading occurred most commonly on the last several questions of an examination. Apparently the examiner placed red dots on the score sheet for each incorrect answer until 30 such red dots had been marked. No further incorrect answers were marked.

The examiners stated that this type of incorrect grading during 1972 was probably the result of nervousness caused by applicants watching them correct the tests. They had no explanation for the continuance of this type of grading for 1973.

Number of Wrong Answers Counted Incorrectly

On many examinations a red dot was placed on the answer sheet for each incorrect answer but then the number of red dots was incorrectly counted. For example, there were 32 red dots on one answer sheet, but the exam was scored 70 percent. (There were 100 questions on the exam.)

There were 30 red dots (giving the applicant a passing score of 70 percent) on another such answer sheet but the exam was scored 69. As a

result of the exam being scored 69, the applicant had to return to Helena from his home on another occasion and retake the exam. The reexamination fee was $10.

Incorrect Percentage Calculation

On some exams with less than 100 questions, the examiners incorrectly calculated the percentage score. For example, one applicant missed 24 questions out of a total of 75 on his examination. His exam was scored 70 percent, but a correct percentage calculation for his score would have been 51 divided by 75, or 68 percent.

The examiners expressed the belief that this type of incorrect grading was due to arithmetical errors.

Unexplained Grading Procedure

The examiners could not explain how one examination was graded. The applicant who took this exam had previously failed the examination three times. The examiner stated that this applicant's employer told them the applicant was knowledgeable but simply could not pass a written exam because testing made him nervous. Under pressure from the applicant's employer, the examiners agreed to give the individual an oral examination. The same exam and answer sheet used for written exams were used for the oral exam. The applicant's exam was scored 78 percent, but there were no combination of marks on the answer sheet which would result in a score of 78 percent or which would result in a passing score of 70 percent. The examiners could not explain how this individual's examination was graded.

We discussed the misgraded examinations with the chief deputy on August 8, 1973, and as a result, the department revised its grading procedures so that the examiner who gave the exams would not also correct the exams.

We reviewed the score sheets for 28 exams given between August 8, 1973, and December 18, 1973. Six of these exams (21 percent) were incorrectly graded. One person who actually scored a 69 was licensed as a result of misgrading. There was no indication that any score sheets had been altered; however, 11 wrong answers were not marked on one score sheet.

Licensing agents who have not passed the examination apparently is a long-standing practice. For example, in March 1961, an applicant took the multi-line exam twice and failed it both times. However, the instructions "issue license" were written on the second exam and the person was licensed.

If the examinations are to serve any useful purpose, they must be graded fairly and impartially and all applicants must be treated equitably.

RECOMMENDATION

We recommend that the department:

1. *Discontinue the practice of altering answer sheets after they have been graded, and grade the exams on an impartial basis.*
2. *Discontinue the practice of not marking wrong answers after 30 such wrong answers have been marked.*
3. *Discontinue the practice of giving oral examinations to applicants who fail the written test, without specific written approval by the commissioner.*
4. *Have all answer sheets reviewed by a second party to assure that all wrong answers have been marked wrong, that the wrong answers have been correctly counted, and that the percentage score has been correctly determined.*

Waiting Period Before Reexamination

Section 40-3314, R.C.M. 1947, provides that the department may require a reasonable waiting period before reexamination of an applicant who failed an examination covering the same kind or kinds of insurance.

The department has not established any criteria as to whether a waiting period should be required or how long any such waiting period should be.

Generally, applicants who fail an examination are reexamined during the next regular examination period. However, some applicants are reexamined the day after failing an examination. For example, one applicant took the exam twice on August 14, 1972, and failed both times. He took the exam a third time on the next day, August 15, 1972, and passed. Some applicants took the same exam on three successive weeks before they received a passing score.

In Idaho, applicants who fail an exam twice are required to wait six months before being reexamined.

The value of the insurance examinations is decreased if applicants can take the test repeatedly until they pass.

RECOMMENDATION

We recommend that the department:

1. *Establish written criteria as to how long a waiting period should be required before reexamination of applicants who fail an insurance examination.*
2. *Require all applicants who fail an examination to adhere to the same waiting period, except in hardship cases specifically approved in writing by the commissioner.*

Frequency of Agent and Solicitor Examinations

Section 40-3314, R.C.M. 1947, requires the department to make examinations available with reasonable frequency and at places reasonably accessible to applicants. The department may make examinations available at its office in Helena at times within the commissioner's discretion, but at least once a month.

The department has no written criteria for determining how often to give examinations or at what locations to give them. Presently, examinations are given weekly in Helena and monthly, except July, August, and September, in Billings. Examinations are also given occasionally, usually on an individual applicant basis, in the department's offices. During 1972, the number of examinations given in Helena ranged from 29 in one week to five in another week. The monthly totals for examinations given in Helena during 1972 ranged from 87 in October to 46 in December. During January 1972, 47 exams were given in Helena during five examination weeks. On three of these examination weeks, less than 10 applicants took the exam.

The department has not analyzed the number of exams given or the locations of applicants to determine whether the frequency of examination or the location at which exams are given need to be revised. The examiners said that exams are not given in Billings during the summer months because few applicants take the exam from that area during the summer, and the roads are good so anybody who wants to take the exam can drive to Helena. Relatively high numbers of examinations were given in Helena during July, August, and September 1972. The department had not determined how many of these applicants came from Billings or surrounding areas, and has not determined whether there are enough applicants from the Billings area to justify giving the exam in Billings during the summer months.

The department should offer examinations at those frequencies and locations which would be most mutually beneficial to license applicants and the state.

RECOMMENDATION

We recommend that the department accumulate statistics as to the number and location of residence of applicants taking the exam, periodically analyze the statistics, and determine the optimum frequency and locations that the examination should be given.

APPROVAL OF INSURANCE FORMS

APPROVAL OF INSURANCE FORMS

Section 40-3714, R.C.M. 1947, requires insurance forms and annuity contracts to be filed with and approved by the department before being issued or used in Montana. Most other states also require similar advance approval of forms.

The department's rates and forms section reviews and approves or disapproves insurance forms filed with the department. The section is staffed by two form reviewers. One reviews life and disability (accident and health) insurance forms, and the other reviews property and casualty insurance forms.

There is no readily available record of the total number of forms presently approved for use in Montana. One form reviewer estimated the number of approved forms to be between 250,000 and 500,000. During 1972-73, 9,305 life and disability insurance forms and 10,398 property and casualty insurance forms were approved. The staff estimates that 10 percent of all forms filed are disapproved on their initial submission.

The insurance law states the department shall disapprove a form only if the form:

-- Violates or does not comply with the code.

-- Contains any inconsistent, ambiguous, or misleading clauses, or exceptions and conditions which deceptively affect the risk purported to be assumed in the general coverage of the contract.

-- Includes any misleading title, or heading, or other indication of its provisions.

-- Is printed or otherwise reproduced in such manner as to render any provision of the form substantially illegible.

The insurance laws also include numerous standard provisions which must be included in various types of policies.

Unapproved Forms in Use

Unapproved insurance forms are being used in Montana.

In addition to copies of approved forms maintained by the rates and forms section, the policyholders' service section maintains samples of several policies which they use to increase their knowledge of insurance contracts and better enable them to assist policyholders. Some of the forms kept by the policyholders' service section were obtained from people with insurance complaints and others were obtained from insurers or their representatives. At the time of our review, the policyholders' service section had samples of 87 insurance forms. Fourteen of these forms (16 percent) had not been approved. Of the 14 unapproved forms, at least six had been issued to Montanans. The unapproved forms included policies, riders, endorsements, and other forms for fire, auto, and life insurance.

During our review we obtained and reviewed 26 insurance forms which were issued in Montana and were presently in force. Five of these forms (19 percent) were not approved for use in Montana.

The chief deputy said there probably are an unlimited number of unapproved insurance forms being used in Montana. He said the department has developed a very limited system to determine if unapproved insurance forms are being used. During the triennial examination of Montana insurance companies, the examiners compare the forms used by the companies against the rates and forms section's list of approved forms. Although out-of-state insurance companies comprise 97 percent of all insurance companies authorized in Montana, there are no procedures to determine whether these companies are using only approved forms. The department's

comparisons of forms used by Montana companies have not disclosed any unapproved forms.

Insurance forms used are not always the same as the forms approved. Upon approval of an insurance form, the rates and forms staff records the form number and approval date. Copies of all approved forms are not kept due to lack of storage space, and the department has no procedures to insure that the forms being used in the state are the same as the forms approved.

We compared 17 forms maintained by the policyholders' service section with copies of approved forms available from the rates and forms section. Two of these forms were not the same as the approved form even though the form numbers were the same. Both of the revised forms had been issued in Montana. In both cases, revisions to the approved forms were advantageous to the policyholder. However, the department has no assurance that other forms have not been revised to the detriment of policyholders.

If form approval is to provide a useful function, the forms used must be the same as forms approved.

Forms approval is a difficult function, primarily because of the large volume of forms, the long duration that many of them remain in effect, and the continuous adoption of new forms. Because of this, it isn't practical for each state to retain an up-to-date copy of each approved form. The answer may be for a national or regional data bank to file the forms centrally for use by the state insurance regulatory agencies. However, pending development of such a system, the department should retain a representative sample of the forms for subsequent verification. In addition, the field examiners should become acquainted with the basic requirements of forms content. This would enable them to determine that proper forms are in use during their

examinations based on this knowledge rather than merely comparing form numbers.

The forms approval requirement provides little policyholder protection unless effective procedures exist to determine if unapproved forms are being used.

RECOMMENDATION

We recommend that the department develop and implement procedures to determine whether unapproved forms are being used.

Title Insurance Forms and Farm Mutual Insurance Forms

Title insurance forms and farm mutual insurance forms are neither filed with nor approved by the department, although the law requires both types of forms to be approved. The commissioner said many farm mutual insurers may have had their forms approved before the department started keeping records of approved forms.

The department has not exempted either type of insurance forms from the approval requirement. On October 9, 1973, the commissioner advised us that the law exampts title and farm mutual insurers from many of the insurance laws and said the failure to require form approval from these insurers was apparently just a departmental oversight. As of December 18, 1973, the department had taken no action to require title and farm mutual insurers to file their forms for approval.

Sections 40-3701 and 40-3714, R.C.M. 1947, require title insurance forms to be approved, and Section 40-4844 requires farm mutual insurance forms to be approved.

RECOMMENDATION

We recommend that the department require title and farm mutual insurance forms to be approved before being used in Montana.

Declaration Pages

Section 40-3718, R.C.M. 1947, requires insurance policies to specify:

-- The names of the parties to the contract.

-- The subject of the insurance.

-- The risks insured against.

-- The time when the insurance takes effect and the period during which the insurance is to continue.

-- The premium.

-- The conditions pertaining to the insurance.

Property and casualty insurance policies generally include declaration pages which summarize this information. Other information also may be contained on declaration pages. Some of the information on the declaration page, such as the risks insured against and conditions pertaining to the insurance, may be discussed in more detail in the policy itself, but other information such as the name of the insured, the period covered by the insurance, and the premium often are shown only on the declaration page. Automobile insurance policies are sometimes renewed simply by execution of a new declaration page.

Property and casualty insurance policies are generally long, technical, and difficult to read and understand. Many policyholders are unable to understand the entire text of their insurance policies. Therefore, they rely on agents and the declaration pages to inform them about their policies.

The department does not require declaration pages to be approved and has not issued an order exempting declaration pages from the approval requirement. However, the reviewer of the property and casualty forms said a former deputy commissioner had given verbal instructions that declaration pages need not be approved.

The declaration page is a part of the insurance policy and is probably the part best understood by laymen. Therefore, declaration pages should be approved by the department in accordance with Section 40-3714.

RECOMMENDATION

We recommend that the department require declaration pages of property and casualty insurance policies to be approved prior to use in Montana.

REVIEW OF ANNUITIES

REVIEW OF ANNUITIES

Annuities are, in essence, a type of savings but are regulated as life insurance and are sold by life insurance companies. Accordingly, the Insurance Department has the responsibility to regulate annuity sales in Montana. Annuity purchasers make single or periodic payments to the insurance company and are guaranteed a specified income at a later date, frequently upon the purchaser's retirement. Generally, the purchaser receives periodic payments after the annuity matures, but most contracts also allow the purchaser to select other payment options. In addition to the basic savings plan, annuities may include other features such as purchase through payroll deductions or postponement of federal income taxes. Annuities are sometimes sold in combination with life insurance.

Under most annuity contracts, a relatively long period is required before the policy's cash value is equal to the purchaser's investment. For example, cash value under one annuity plan extensively sold by a Montana company was less than the required investment for more than 10 years after the purchase date.

Annuities often include numerous complex options affecting a purchaser's costs and benefits. A review of the department's complaint files and discussion with annuity purchasers show that there is often a lack of communication between the seller and purchaser at the time of annuity purchases. Many purchasers apparently don't fully understand their annuities at the time of purchase. One such purchaser said he was led to believe that he would receive a return at a high interest rate after making payments on an annuity for two years. When the high interest return did not materialize, he surrendered his policy for a partial refund. He had invested over $1,000 and his refund was for about $400. Another

purchaser said he invested over $1,700 in an annuity and also surrendered the policy when the anticipated high interest rate return did not materialize after two years. This purchaser eventually obtained a full refund after threatening to sue the company. Another purchaser bought an annuity with the understanding that she could withdraw the money at any time. When a need for the money arose, she learned she could not obtain a full refund. As of November 1973, none of her $500 investment had been returned. Another purchaser said he invested $5,000 under the impression he could withdraw the money at any time.

Annuity contracts generally are not delivered to the purchaser until several weeks after purchase. Therefore, at the time of sale, purchasers must rely upon the agents to fully explain contractual features. In some instances the agent may not fully explain all conditions and limitations of the contract.

Annuity purchasers should be aware of the features in the contract to be purchased. Insurance companies should be required to furnish disclosure statements to annuity purchasers before the contract becomes binding. A disclosure statement would inform the potential purchaser of all the salient features, including limitations, of the annuity contract. The State of Wisconsin, for example, presently requires disclosure statements for the sale of annuities.

RECOMMENDATION

We recommend that the department seek legislation requiring insurance companies to furnish disclosure statements on forms approved by the department before the sale of annuity contracts.

EXAMINATION OF INSURERS

EXAMINATION OF INSURERS

Section 40-2713, R.C.M. 1947, requires the department to examine the affairs, transactions, accounts, records, and assets of each authorized insurer at least once every three years. For out-of-state insurers, the department may accept the last recent examination report of the other state's insurance regulatory agency in lieu of conducting its own examination.

Examinations are a part of the department's responsibility to regulate the insurance industry for the public protection. The main purpose of examinations is to independently verify the accuracy of insurance companies' annual financial statements. The primary need for the examinations is to determine the companies have sufficient resources to honor their policies. Other purposes of examinations are to review insurance forms, determine whether companies' operations are in the public's interest, and to determine whether companies paid the correct amount of tax.

To eliminate duplicate examinations of multi-state insurance companies, the 50 state insurance regulatory agencies participate in a regional examination system sponsored by the National Association of Insurance Commissioners. Under this system, examinations of multi-state companies are conducted jointly by representatives from several states in which the company does business. The commissioner from each state in which the company is authorized usually accepts the report of the joint examination, but retains the authority to conduct a separate examination if he believes it is necessary. Montana has six examiners who participate in joint examinations.

Most Montana insurance companies are relatively small and conduct most or all of their business in Montana. These companies are usually examined by the department's examination staff which consists of a chief examiner and six field examiners. The chief examiner, however, has numerous other

responsibilities and devotes only a small part of his time to the examination of insurance companies.

During 1972, the examiners examined one Montana company and participated in 22 examinations of out-of-state companies.

Examiners' Independence

The purposes of examinations are to independently verify the accuracy of insurers' financial statements and to independently determine whether insurers are financially strong enough to meet present and anticipated future claims of policyholders. The value of examinations is questionable unless the examiners are totally independent of the company being examined. Independence not only means that the examiner must not have any financial, managerial, employment, or ownership involvement in the company being examined, but also means the examiner must be independent in mental attitude. Without complete independence, the examiner may be biased in his evaluation of a company's operations.

Montana's six field examiners are not state employees in the sense they're normally construed. The examiners are paid per diem wages, travel expenses, and living allowances directly by the companies examined. The chief examiner is a state employee and is paid by the state. However, companies examined are billed for the chief examiner's time and expenses, and the money collected is deposited in the state's General Fund.

Section 40-2717, R.C.M. 1947, requires insurers to bear the costs of examinations but does not specify the method of payment. Section 40-2717 (2) states:

> "The commissioner shall pay to the state treasurer to the credit of the general fund all moneys received pursuant to subsection (1) above." (Subsection (1) requires insurers to pay examination costs.)

This indicates the intent that the state be reimbursed for examination costs it incurs as opposed to the insurance companies paying the examiners directly. Because the field examiners are paid directly by the insurers, no money is collected by the state for the field examiners' services.

Field examiners are appointed by the commissioner but are not on the state payroll. They receive no state salary and do not participate in the state retirement system or other employee benefits. The examiners' only compensation for examinations conducted is the per diem wage paid directly by the company examined.

The examiners' independence would be enhanced if they were state employees whose salaries were not contingent upon the number of days spent at each insurer's office. The trend is for the state regulatory agencies to employ their examiners directly. Over one-half of the states now use state employed examiners.

RECOMMENDATION

We recommend that the department require all examiners to be salaried state employees and seek the necessary appropriation to pay the examiners.

Examination Guidelines and Workpapers

Examiners should have an examination guideline or checklist to initial or otherwise indicate they have completed each necessary examination procedure. In addition, they must gather sufficient evidence to satisfy themselves of the accuracy of the statements being examined. This evidence is usually accumulated in workpapers.

The department doesn't have an examination checklist. This increases the possibilities for overlooking necessary examination steps. The National

Association of Insurance Commissioners has set forth in its publications many of the necessary examination procedures. The department could use these procedures as the basis to start development of an examination checkoff list.

The department's workpapers for several examinations of Montana insurance companies were inadequate. For example, the workpapers for the last examination of one company contained no evidence that the examiner had

-- Reconciled the cash accounts, even though bank confirmations from four banks showed more cash on hand than was reported in the financial statements and there was no confirmation from a fifth bank.

-- Verified policyholder loans.

-- Verified investments in bonds even though bonds accounted for the majority of the company's assets.

-- Verified mortgages.

-- Verified share deposits in saving and loan associations.

-- Inspected property deeds.

-- Verified expenses payable.

The examination report stated that many of these verifications had been made, and the chief examiner said all verifications had been made. However, he said workpapers were not prepared to specifically indicate these procedures had been performed. He concluded that "all pertinent workpapers are kept; only scrap papers are destroyed." The above listed procedures are basic audit procedures for which workpapers should be prepared to show the extent the procedures were employed, any problems noted, and disposition of the problems.

Workpapers contain the examiner's only evidence to support his examination report. Their purpose is to show what audit work has been done, what methods and procedures were followed, and what conclusions were reached. Workpapers provide the examiner with the evidence for his report and document the adequacy of the examination in the event the company should subsequently become insolvent. Workpapers are basic to any audit activity, including independent audits by public accountants and governmantal entities, and internal audits within industry, government, and other organizations.

We polled several other states to determine whether their examiners prepare workpapers. Fifteen states responded to our questionnaire, and each said examination reports were supported by workpapers. All responding states also said workpapers were retained, either until the next examination or for a specified time period.

RECOMMENDATION

We recommend that the department:

1. *Develop an examination procedure checkoff list and require the examiners to initial each procedure upon its completion during the examination.*
2. *Prepare and retain adequate working papers for each examination conducted.*

Extent of Examinations

Examinations are primarily an independent verification of an insurer's financial statements, but the audit should not be limited to the statements or the insurer's accounting records. Examinations should include physical inspection of assets and gathering of evidence from outside sources, such as banks, debtors, mortgagors, and issuers of securities.

Montana examiners are not obtaining sufficient evidence to verify some items on insurers' financial statements. For example, during a recent examination of a Montana insurance company, the examiner did not verify policyholder loans with the policyholders, and real estate mortgages were not verified with the mortgagor or with county records. The examination was limited to information in the company's books. The chief examiner said securities, loans, mortgages, and other similar assets are not verified to outside sources as a normal procedure.

Most insurers invest a large part of their assets in securities such as stocks, bonds, and mortgages; therefore, the examination of these securities should be quite thorough.

The collapse, in 1972, of a large insurance company which was authorized in Montana demonstrates the need for in-depth examinations. After the company collapsed, examiners could locate only about $4 million out of $24 million in reported securities.

The department's working papers that we reviewed do not show that examinations of Montana insurers included verification of income and expense. Income and expense amounts should be verified to satisfy the examiner that unreported liabilities do not exist and that the net profit or loss transferred to the balance sheet as unassigned surplus is correctly stated.

Without verification of the income and expense accounts, a company could be going broke and the examiner would be unaware of it. Also, the insurance laws (Section 40-3640, R.C.M. 1947) state that insurance rates may not be excessive, inadequate, or unfairly discriminatory. Verification of the income and expense accounts could help the department evaluate insurance rates.

RECOMMENDATION

We recommend that the department:

1. *Extend its examination procedures to include confirmation from outside sources where appropriate.*
2. *Extend examinations to include verification of income and expense accounts.*

Coordination With Other Independent Audits

Most insurance companies have their records audited by independent public accounting firms. Many of the examination procedures the department's examiners should be employing are utilized by the public accountants in their audits. The department currently does not coordinate its examination efforts with the public accountants' audits. It is likely the examiners may be able to limit their examination procedures in many instances if the public accountants have already performed the work. Accordingly, the department should pursue the possibilities of doing so.

RECOMMENDATION

We recommend that the department coordinate its examinations with audits of the same companies conducted by independent public accounting firms.

REGULATION OF INSURERS' SECURITY DEPOSITS

REGULATION OF INSURERS' SECURITY DEPOSITS

Section 40-2809, R.C.M. 1947, requires insurance companies to maintain deposits of securities for the protection of policyholders and creditors.

Security deposits are administered in three different ways. Most Montana insurers deposit the securities in banks through the department. Deposits are kept in safe deposit boxes and the department has one key and the insurer or its agent, which in many cases is the bank, has the other. The commissioner has delegated the duty of deposit administration to his chief examiner. Other insurers establish a trust through a bank, and the bank periodically certifies, to the department, the amounts being held. Out-of-state insurers commonly deposit securities with the insurance regulatory agency of their home state. These agencies then issue certificates to the Montana Insurance Department stating that a certain amount is on deposit in their state for the protection of all the insurers' policyholders.

Fourteen insurers have deposits totaling $40 million subject to the department's control. Of this amount, $34 million is administered by trust arrangements with banks, and the remaining $6 million is being kept in safe deposit boxes accessible to the department. The department's consent is required for the deposit and withdrawal of all securities under its control.

We did not determine the amount of securities held in other states for policyholder protection.

The amounts of deposit required for different types of insurance are listed below.

Type of Insurance	Minimum Deposit Requirement
Life	$100,000
Disability	100,000
Life and Disability	150,000
Property	200,000
Marine	200,000
Casualty (except workmen's compensation)	200,000
Casualty (including workmen's compensation)	300,000
Surety	250,000
Title	50,000
Multiple Lines (2 or more: casualty, property, marine, or surety)	400,000

Montana life insurance companies are required to maintain deposits equal to the reserves on outstanding life insurance policies and annuity contracts; however, their minimum deposit requirement may be credited to this deposit. Annually on or before April 1, each Montana insurer must deposit additional securities to bring its deposit up to an amount equal to the reserve liabilities on outstanding life insurance policies and annuity contracts as of December 31, of the preceding year.

Deposit Records

Section 40-3205, R.C.M. 1947, requires the department to keep records of each deposit, showing as far as practical the amount and market value of each item, and all transactions relative to the deposit.

The department does not maintain adequate records of deposited securities. The files of insurers' deposits consist of deposit and withdrawal forms and a schedule that is supposed to list each transaction and show a running balance; however, the schedules are not current. The balance

in each deposit cannot be determined without reviewing transactions that took place since the last recording. For example, the last entry for one insurer's deposit record was made on January 13, 1970. Approximately 50 securities had been deposited or withdrawn since then.

The department also has no record of the present value of securities deposited by each insurer.

Without adequate records the department has no assurance that sufficient securities are on deposit.

RECOMMENDATION

We recommend that the department implement a system of accounting for insurer deposits that will provide current and complete records.

Internal Control of Deposited Securities

The department holds about $6 million worth of stocks, bonds, deeds, mortgages, and certificates of deposit owned by insurance companies. The securities are held in safe deposit boxes located in various Montana banks. Some of the bonds are bearer bonds.

Duties for handling of insurer deposits are not separated. The chief examiner maintains and controls all records, approves and makes deposits and withdrawals of securities, has access to safe deposit boxes, performs any inventory of securities, and clips interest coupons.

Adequate internal control procedures require separation of the recording and custodial responsibilities. Separation of duties is essential for adequate internal control of assets. This need increases with the liquidity of the assets and is especially important when the assets in question are being held in trust for others.

As discussed on page 74, records of deposits are not adequate. One measure of good internal control is the accuracy and reliability of accounting and operating records.

RECOMMENDATION

We recommend that the department implement a system of internal control that establishes clear lines of authority, responsibility, and provides the necessary separation of duties.

Valuation of Deposits

Section 40-3212, R.C.M. 1947, requires deposited securities to be valued at market value. In addition, the National Association of Insurance Commissioners has established security valuation guidelines for financial statement purposes which, if followed, would generally result in valuation at or near market. The N.A.I.C. guidelines were intended to result in uniform valuation methods so that each state may rely on the other's valuations. These guidelines could be used in valuing deposited securities.

Insurance companies value and report deposited securities at a mixture of par values, amortized book values, and present values. This mixture of values is almost useless in determining the true value of the deposits. The department does not follow N.A.I.C. guidelines and accepts the companies' valuations. It does not determine the market value of deposited securities to assure the minimum deposits have been made as required by law.

As discussed on page 74, the department doesn't keep current or complete records of securities on deposit. Therefore, we reconstructed the deposit records for three insurance companies. We then valued stocks and bonds, using the N.A.I.C. recommended approach for determining market values or

cost plus amortization as indicated in the companies' annual financial statements. Mortgages were valued according to the amount of the outstanding principal.

Deposits for all three companies were less than those required. One insurer was required to maintain a deposit of $400,000, and reported deposits equaling or exceeding that amount. However, the market value of securities on deposit for the 5-1/2 year period from December 1965, to June 1971, was never sufficient to meet statutory requirements. The deficiency ranged from $88,000 - $93,000 over this period. Another insurer was required to have a minimum deposit of $100,000, but because it was a life insurer, it was also required to have a deposit equal to its reserve on outstanding life insurance policies. The deposits of this insurer were deficient in amounts ranging from $37,300 to $81,500 over the five-year period, April 1968 to April 1973. The chief examiner said the securities for these companies had been recorded at par value and the companies met the deposit requirements. He said he didn't determine the market value of the companies' security deposits.

Valuation of securities at par value is insufficient because par is seldom an indication of a security's actual value. Valuation at par deprives the public of the needed protection as recognized by the law which requires valuation at market value. The department should value at market deposits that it holds and require trustees and insurance regulatory agencies of other states to annually report the market value of security deposits held.

RECOMMENDATION

We recommend that the department value securities at market and establish a system for periodic evaluation of securities on deposit.

Notice of Deposit Deficiency

Section 40-3212, R.C.M. 1947, requires the department to revoke the certificate of any company which has deficient deposits if the deposits are not brought up to the required amount within 20 days after receipt of the department's notice of deficiency. Deficiency notices are to be made by registered mail.

The department does not notify, by registered mail, insurance companies whose deposits are deficient. For example, one insurer had a certificate of authority to transact life and disability insurance from March 1967, to March 1972, when the company reinsured all its life business, gave up its certificate to transact life and disability insurance, and acquired a certificate to transact multiple lines of property and casualty insurance. Following is a schedule showing the deposit deficiency of this insurer.

Date	Deposit Required	Actual Deposit(1)	Deposit Deficiency
3/1/67	$150,000(2)	$ 51,709	$98,291
4/1/68	150,000	55,653	94,347
4/1/69	150,000	59,598	90,402
4/1/70	150,000	63,543	86,457
4/1/71	166,583(3)	67,488	99,095
4/1/72	400,000(4)	312,165	87,835
4/1/73	400,000	313,000(5)	87,000
10/2/73	400,000	315,000(5)	85,000

(1) Market values or approximations thereof.
(2) Minimum deposit for insurer of this type - Section 40-2809.
(3) Increase due to reserve requirement - Section 40-3012.
(4) Increase due to insurer becoming a property and casualty (multi-line) company - Section 40-2809.
(5) Estimated.

Annual financial statements of this insurer for the years 1968 through 1971, disclosed the deposit deficiency. The examination report for the three-year period ending December 31, 1970, reported the deficiency. In addition, a letter dated June 25, 1971, between officers of the company, a copy of which was sent to the commissioner, suggested the company knew its deposits were deficient. However, neither the company nor the department took any action to increase the deposit until March 31, 1972, when the company converted from a life to a property and casualty insurer and deposited additional securities because of the higher deposit requirement for property and casualty insurer. However, as shown in the preceding schedule, the deposits still were not adequate to meet requirements for this insurer. In its entire history, the company never had enough on deposit.

The department never notified this company by registered mail that its deposit was deficient. The chief examiner said the deficiency disclosure in the examination report served as official notice to the company. However, the department did not revoke the company's authority and never required the company to increase its deposit.

The chief examiner said he presently isn't concerned with the deficient deposit because the company is no longer writing insurance. However, the company had premium income of over $900,000 for the five-year period 1967 through 1971, and should have had adequate deposits during that period.

Deposits are required to provide policyholder protection in the event insurers become insolvent. Policyholder protection is inadequate unless deposits are maintained at required levels.

RECOMMENDATION

We recommend that the department:

1. *Promptly notify, by registered mail, companies with deficient deposits.*

2. *Require all companies whose deposits are deficient to increase deposits to required levels.*

3. *Revoke certificates of authority of all companies that, after notification, don't increase their deposits to the required levels.*

COLLECTION AND DISTRIBUTION OF PREMIUM TAXES

COLLECTION AND DISTRIBUTION OF PREMIUM TAXES

Section 40-2821, R.C.M. 1947, requires insurance companies doing business in Montana to pay taxes on insurance premiums collected. Premiums collected are taxed at the rate of 2-3/4 percent except that an additional 3/4 of one percent is assessed on fire insurance premiums. Marine insurance is taxed at the rate of 3/4 of one percent of gross underwriting profit rather than the 2-3/4 percent premiums assessed on other types of insurance. For the year 1972, the department's records show insurance companies paid premium taxes totaling $6,403,417 to Montana.

Collection and verification of premium taxes is a function of the department's chief examiner.

In-Lieu Nature of Taxes

Section 40-2821, R.C.M. 1947, states that with respect to insurance companies, premium taxes are in lieu of all other state and local taxes except property taxes and taxes for the support of the state fire marshal program. This provision enables an organization to incorporate as an insurance company, do little or no insurance business, invest its resources in other operations, and pay little or no tax.

One Montana insurance company has invested in real estate and, to the extent necessary to meet insurance deposit requirements, in securities. In 1972, the company collected insurance premiums totaling $755,384 and had a net investment income of $199,215. The company paid no state income taxes on its investment income. Another Montana insurance company wrote no insurance during 1972, but had investment income of $43,671. The company paid no premium taxes or state income taxes for 1972.

Section 40-2821, R.C.M. 1947, exempts considerations received on annuity contracts from taxation. Many other states, including South

Dakota, California, Maine, West Virginia, and Florida tax annuity considerations. Some states tax them at the same rate as life insurance, some tax them at higher rates, and some at lower rates.

Annuities constitute a large part of some companies' business in Montana. For example, during 1972, one company collected $253,000 in annuity considerations from Montanans. These annuities accounted for 49 percent of its Montana business.

Annuity considerations should be subject to the premium tax because no other taxes are assessed against annuity considerations or the income derived therefrom. The department's records show that insurance companies collected about $5 million of annuity considerations in Montana during 1972. Tax, at 2-3/4 percent, on that amount would be $137,500.

It seems unreasonable that insurance companies pay no taxes on income earned from non-insurance operations when other businesses pay taxes on such income.

RECOMMENDATION

We recommend that the department explore the feasibility of requesting legislation to amend Section 40-2821, R.C.M. 1947, to provide for taxation of non-insurance income and annuity considerations.

Limitations on Insurers' Investments

Montana insurance laws limit the types of investments insurance companies may make. Section 40-3128, R.C.M. 1947, limits insurers' investments in real estate held for the production of income to an amount not exceeding, without the commissioner's consent, five percent of its assets.

The five percent limitation on real estate investments has two primary benefits to the public. It preserves insurers' liquidity so they will be able to meet policyholders' claims, and it limits the amount of tax-free income insurers could make from large investments. As previously discussed, insurance companies are not subject to state income taxes.

One Montana company had 19.5 percent of its assets invested in real estate as of December 31, 1972. The real estate consisted primarily of a large ranch held for subdivision. The insurance company owned about one-half of the ranch directly and the other half was owned by the insurer's wholly-owned subsidiary. On October 28, 1971, the company obtained the commissioner's consent to exceed the five percent real estate limitation.

The commissioner advised us he was unaware of the reason(s) for or the legislative intent of limiting insurers' real estate investment. He said he granted the exception because the ranch, subdivided, was going to be an extremely profitable investment for the company. To assure policyholder protection and consider the tax equity, the commissioner should develop and apply written criteria for granting a significant exception to the statutory limitation.

Information in the department's files shows that subsequent to our review, title to all of the ranch property was transferred to a newly incorporated development company which is wholly owned by the insurance company's wholly-owned subsidiary. The insurance company holds a promissory note and first mortgage for its prior direct land holdings. As a result of these transactions, it is estimated the insurance company stands to gain about $800,000, which will not be taxable to the company or its subsidiary.

RECOMMENDATION

We recommend that the department establish written criteria for use in determining whether exceptions should be granted to the five percent limitation on real estate investments.

Tax Collection Period

Premium taxes are assessed on a calendar year basis. Section 40-2821, R.C.M. 1947, requires the taxes to be paid by March 1 for the preceding year.

Many states, including California, Indiana, Minnesota, Wisconsin, Florida, and New York require quarterly installments on premium taxes and a year-end reconciliation. Since companies doing business in these other states must compute the premium taxes quarterly, consideration should be given to requiring quarterly payments of premium taxes in Montana.

We estimate Montana could realize annual interest income of about $170,000 by requiring quarterly installments for premium taxes. Because more than 99 percent of premiums collected in Montana are collected by out-of-state companies, nearly all of this amount would result from quarterly payments by out-of-state companies. This income should far offset any additional cost the department would incur to process the more frequent collections.

RECOMMENDATION

We recommend that the department consider proposing legislation to amend Section 40-2821, R.C.M. 1947, to require quarterly installments of insurance premium taxes.

Premium Tax Forms

Each insurance company is required to file an annual report showing the amount of insurance premiums collected during the year and to pay the premium tax thereon. Each year the department furnishes forms for reporting premiums and calculating the tax payable. Property and casualty insurers receive one form, and life and disability insurers receive a different form.

Premium taxes are computed on premiums collected as shown in each company's annual financial statements. The tax form for property and casualty insurers instructs the companies as to which line items on the financial statements are to be entered on the tax report form. The tax form for life and disability insurers doesn't include similar instructions, and different companies are reporting life and disability premiums on different bases. For example, the tax form includes one line for reporting all life and disability premiums and does not instruct insurers which lines on their financial statements should be reported as life and disability premiums. Some companies include annuity considerations in their reported premiums and others do not. Therefore, some companies pay taxes on annuity considerations and others do not. As discussed on page 81, Montana law presently exempts annuity considerations from taxation.

The tax form for property and casualty insurers includes space for the computation of taxes on marine insurance, but the form shows an erroneous tax rate. The tax rate for this type of insurance is 3/4 of one percent (.0075) of gross underwriting profit, but the tax form states "Premium tax .0075% of Gross Underwriting Profit $____." The forms should state 3/4 of one percent, or .0075, rather than .0075% which converts to .000075. The form has been in error since at least 1962.

Some companies compute the tax at .000075 as instructed by the form, and others compute the tax at .0075 as provided by law. Some companies even strike out the incorrect rate shown on the form and insert the correct rate.

The amount of marine insurance premiums collected in Montana is relatively small (about $80,000 during 1972), therefore the tax underpayment caused by the incorrect form is not large. One company paid a marine insurance tax of $.05 for 1972, when it should have paid $5.

Premium tax forms prescribed by the department should be accurate, complete, and easy enough to understand to assure that all insurers compute their tax correctly and that all insurers are taxed on an equal basis.

RECOMMENDATION

We recommend that the department:

1. *Revise the life and disability insurance tax form so that all insurers are aware of which premiums are taxable and which are not.*
2. *Revise the property and casualty insurance tax form to reflect the correct tax rate for marine insurance.*
3. *Periodically review tax forms to determine whether they are still appropriate.*

Verification of Premium Tax Payments

After receiving the annual premium tax reports, tax payments, and annual financial statements, the chief examiner verifies the tax payments.

We reviewed the 1972 premium tax payments of 68 companies and found that 15 (22 percent) paid an incorrect amount of tax. The incorrect

payments in this limited test consisted of both underpayments ($5,296) and overpayments ($1,749). Some of these erroneous payments are discussed below.

One insurance company, a Montana company, submitted a premium tax report for 1972 that showed significantly less premium collections than was shown on its annual financial statement. The company paid a premium tax of $10,386, based on premium collections shown on its tax report. The chief examiner informed the company its premium tax calculation was incorrect and the company submitted a revised tax report and paid an additional $5,047 of taxes. Premium collections shown on the revised tax report agreed with one figure shown on the financial statement, but that figure excluded taxable deferred premiums and included non-taxable annuity considerations and premiums collected in other states which are not taxable in Montana. However, the chief examiner accepted the revised tax calculation "until the next examination fo company." After the two payments the company still underpaid its 1972 premium taxes by as much as $5,426. Conflicting data in the financial statements precludes a determination of the exact amount without further information. During 1972, the company converted over $100,000 in annuity contracts to life insurance policies. The annuities were sold during prior years and no tax was paid on annuity considerations received during these years consistent with the law. The company claims the 1972 life insurance premiums collected through conversion of annuity contracts are not taxable because no money was collected during 1972. However, the premiums appear to be taxable because they represent life insurance premiums collected in 1972 and because no tax was paid on the premiums when the company collected them. A legal determination should be sought to clarify the matter. Even if the disputed premiums were not taxable, the company still would have underpaid its 1972 taxes by over $2,300.

The chief examiner said this company's tax computation was not based on financial statement data, but he was sure the revised tax was within $100, one way or the other, of the correct tax. At any rate, he said he was not worried about the tax payment because the examiners would catch any errors during their next examination of the company. However, this company and its predecessor underpaid its premium taxes in previous years and the underpayments were not disclosed by the last examination of the company. The company underpaid its 1971 premium tax by $302, and possibly also underpaid its 1970 and 1969 premium taxes. Conflicting data in the financial reports precludes a timely determination of the correct taxes for 1969 and 1970. In 1972, the company was examined for the three-year period ending December 31, 1971, but the examination did not disclose the underpayments. There was no evidence in the examination workpapers that the examiners had even checked the premium tax payments.

Another Montana company underpaid its premium tax by $256 for 1969. The company was examined in 1970 for the three-year period ending December 31, 1969, and the examination did not disclose the underpayment. Again, the workpapers showed no evidence that the examiners had checked premium tax payments.

The handbook of the National Association of Insurance Commissioners points out that premium tax payments should be verified. Inclusion of such a procedure on the examination checklist discussed earlier would require the examiners to address the subject in their examinations.

The premium tax underpayments disclosed by our review were based on information reported in the companies' annual financial statements and should have been disclosed during the department's premium tax verifications, and subsequent examinations in those instances when they were conducted.

Several out-of-state companies overpaid their 1972 premium taxes because they included annuity considerations as taxable premiums. (As discussed on page 81, annuity considerations presently are not taxable in Montana.) The following list shows examples of these overpayments:

Company	Tax Payment	Tax Liability	Overpayment
A	$ 3,791	$ 3,441	$350
B	24,573	24,205	368
C	88,121	87,351	770

Other companies overpaid their 1972 premium taxes because of mathematical errors. For example, one small company had taxable premiums of $2,107 in Montana. The tax should have been $57.94; however, the person who computed the tax misplaced a decimal point and the company paid $579.38, an overpayment of $521.44.

The chief examiner said he was aware that some companies overpaid their taxes; however, he said he is only interested in making sure the state receives enough tax. No action was taken on overpayments unless the companies subsequently recognized the overpayment and requested refunds. Companies which requested refunds were allowed to deduct the overpayments from the next year's taxes. No cash refunds were made.

The chief examiner said cash refunds are not made because he believed once the tax receipts have been deposited in the General Fund, there is no way to get the money out without an appropriation. However, this is incorrect because Section 79-415(3), R.C.M. 1947, provides that:

> "Money paid into the state treasury through error or under circumstances such that the state is not legally entitled to retain it, and a refund procedure is not otherwise provided by law, may be refunded upon the submission of a verified claim approved by the state controller."

The state should collect all premium taxes due from each insurance company. However, the state has no right to overpayments and should refund

overpayments immediately without specific requests.

RECOMMENDATION

We recommend that the department:

1. *Seek a legal opinion on the taxability of the annuity contracts converted to life insurance policies.*
2. *Recover the underpayments from companies whose prior premium tax payments were deficient.*
3. *Include the procedure of verifying premium tax payments on the examination procedures checklist.*
4. *Refund all tax overpayments, including retroactive refunds, without requiring the company to request such refund.*

Premium Tax Distributions

Each year a portion of the premium taxes collected are distributed to relief funds of fire and police departments of Montana communities. The moneys augment local tax moneys which are used to pay firemen and policemen pensions and to provide relief to injured firemen and policemen. Distributions to local fire and police departments are governed by Sections 20-2726, 11-1919, 11-1920, and 11-1834, R.C.M. 1947.

First class cities and towns receive distributions for firemen's relief funds equal to 10 percent of the firemen's compensation for the preceding year. Second class cities and towns also receive firemen's relief fund distributions of 10 percent of firemen's compensation unless that distribution would be less than 25/100 mills of the town's assessed valuation. In the latter instances, second class towns receive distributions equal to the premium tax paid on the fire insurance portion of premiums collected in each city or town. Incorporated cities and towns, other than first

or second class, which have organized fire departments, also receive distributions equal to the premium tax on fire insurance sold in the town.

Section 11-1918 requires each insurer to annually report the amount of the fire portion of premiums received by it during the preceding year in each incorporated city or town. These premium allocations are the basis for tax distribution to most second class and other incorporated cities and towns except first class cities.

Allocating the fire insurance portion of premiums collected to each city or town can be a sizable undertaking for insurance companies. Allocations reported are not always complete or accurate and result in premium tax distributions which are not always fair and equitable. For example, a company might sell fire insurance for property located in one town but allocate the premiums to a nearby city because that is the location of the selling agent's office. The town would then be deprived of its fair tax distribution. Likewise, fire insurance premiums for rural farm property near a town might be allocated to that town because the agent's office is located there. The town would then receive more than its fair tax distribution. The following schedule shows examples of the wide disparity in firemen's relief fund distributions to towns of similar population and with similar assessed valuations.

Town	Population	Assessed Valuation	1972 Firemen's Relief Fund Distribution	1972 Distribution Per Fireman
"A"	1,651	$6,942,610	$ 698.00	$ 25.85
"B"	1,873	6,255,800	1,771.05	110.69
"C"	1,097	1,875,600	368.52	13.16
"D"	717	1,896,472	939.84	40.86
"E"	714	1,471,854	2,172.94	103.47
"F"	663	1,477,054	881.75	31.49
"G"	2,652	8,400,817	27,188.43	971.02
"H"	3,349	8,332,268	3,541.98	141.68

The distribution to Town "G" included taxes paid for fire insurance written on a large industrial plant located near the town but not within the fire district serviced by the town's fire department. The industrial plant provides its own fire protection.

Distributions are made to local police department relief funds in amounts equal to the town's firemen's relief fund distribution. Accordingly, the inequities found in distribution to fire departments also exist in the distribution to police departments.

The following table shows examples of the disparity of distributions to police departments.

Town	Population	Assessed Valuation	1972 Policemen's Relief Fund Distribution	1972 Distribution Per Policeman	1972 Distribution as a Percent of 1972 Policemen's Salary
"A"	1,651	$ 6,942,610	$ 689.00	$ 349.50	5.9
"B"	1,873	6,255,800	1,771,05	1/	1/
"C"	1,097	1,875,600	368.52	368.52	not determined
"D"	717	1,896,472	939.84	469.02	8.7
"E"	714	1,471,854	2,172.94	2,172.94	35.0
"F"	663	1,477,054	881.75	881.75	16.3
"G"	2,652	8,400,817	27,188.43	4,531.41	57.6
"H"	3,349	8,332,268	3,541.98	590.33	7.9
"I"	9,023	26,185,059	13,516.55	965.47	12.1
"J"	6,883	21,820,104	7,720.47	857.83	10.8

1/ Not computed. Town and county have a combined city-county law enforcement organization.

There is no rational reason for the wide variances in distributions per policeman.

Distributions to local firemen's and policemen's relief funds should bear some relationship to the firemen's and policemen's needs or activities. In our previous report on the administrative services program of the State Auditor's Office we recommended that the State Auditor's Office seek

legislation to eliminate conflicting statutory provisions and clarify others relating to the distributions to fire and police pension funds. Any legislative revisions should set forth the purposes for these distributions and establish distribution systems which will equitably achieve the intended purposes.

RECOMMENDATION

We recommend that the department review the statutes relating to premium tax distributions and propose legislative changes necessary to clarify the intent of these distributions, eliminate conflicts in the statutes, and establish fair and equitable distribution procedures.

ACTION ON

INSURANCE COMPLAINTS

ACTION ON INSURANCE COMPLAINTS

Each year many insurance complaints are filed with the department. Review of these complaints is a function of the policyholders' service section, which consists of a supervisor and two investigators. During 1972, the department's records show receipt of 1,165 complaints. Of these, the records show 734 were resolved in favor of the complainant, 429 were resolved in favor of the insurance company, and two were unresolved at year-end.

Records of Complaints

Each complaint received is recorded in a log which the investigators use to show the status of complaints, e.g., resolved or still needing action. At the end of each month the policyholders' service section supervisor prepares a list of complaints received. The list is alphabetized by insurance company and shows the name of the company involved, the name of the complainant, the type of insurance involved, the nature of the complaint, and the initials of the investigator. A monthly recap of complaints is prepared which summarizes complaints by type of insurance and shows the number resolved in favor of complainants and the number resolved in favor of insurance companies.

In many instances, the determination as to whether a complaint was resolved in favor of the complainant or in favor of the insurance company is questionable. For example, there was no indication in one complainant's file that the complaint had ever been resolved. However, this complaint was marked on the monthly list as being resolved in favor of the complainant. The policyholders' service section supervisor said he assumed the complainant obtained a satisfactory settlement because the complainant did not continue to correspond with the department. He said he had to make a determination

that it was resolved in favor of one party or the other so he marked it resolved in favor of the complainant. In another case, the department was unable to assist a policyholder in resolving his complaint. A letter sent to this complainant stated, "We regret we are unable to be of assistance in this matter." This complaint was also marked on the monthly list as being resolved in favor of the complainant. The supervisor stated that he was aware the complaint was not resolved in favor of the complainant, but he had no way to mark it as the complaint also was not resolved in favor of the insurance company.

Insurance complaint records, particularly the monthly list of complaints, if accurately maintained, would be a valuable source of information regarding insurance practices in the State of Montana. Additional status or resolution categories should be established if the existing two are inadequate.

RECOMMENDATION

We recommend that the department make accurate determinations as to the disposition of complaints.

Complaint Handling Procedures

Nearly all complaints filed with the department are investigated through telephone conversations and an exchange of correspondence. Typically, upon receipt of a complaint, the department writes to the insurance company involved, sends it a copy of the complainant's letters, and asks the company to review the situation and advise the department of any actions taken. Upon receipt of a reply from the company, the department writes to the complainant enclosing a copy of the insurance company's

letter and stating that the complaint has been resolved in favor of the complainant if that is the case, or explaining that the company had acted in accordance with the contract and therefore no further action could be expected. Normally, complaints are not investigated except through this exchange of correspondence procedure.

One complaint, filed in March 1973, involved a life insurance policy which was held out to be a policy to provide for funeral and burial expenses. The complainant stated a mortician had advised him the policy probably was illegal. The investigators did not determine the form number of the policy involved, whether the policy form had been approved by the department, nor whether the policy was legal or illegal.

Another complaint filed in April 1971, involved an annuity. The complainant alleged that the agent misrepresented the policy at the time of sale. The complainant stated the agent informed him that after two years he could withdraw all money paid into this plan. Later, he discovered that the policy did not provide for such 100 percent withdrawal, and requested the company to refund the premiums on the basis of misrepresentation by the agent. When the company refused to refund the premiums, the policyholder complained to the department. The complainant sent the department a statement signed by five other people stating that the agent misrepresented the policy to all of them in a group meeting.

The policyholders' service section staff did not perform a field investigation of this complaint or conclude whether the agent had misrepresented the policy.

In May 1971, another complaint involving alleged misrepresentation by the same insurance agent was filed. Again, no field investigation was made. In 1972, four complaints involving alleged misrepresentation

by this insurance agent and his staff were filed with the department. No field investigations were made on the alleged misrepresentations; however, the agent and his staff were called into the departmental offices to explain their sales presentation. The policyholders' service section supervisor said he could detect no misrepresentation. However, he said he had no way of knowing what the agents actually told potential clients. During 1973, eight complaints involving alleged misrepresentation by this agent and his staff were filed with the department.

Policies sold by these agents involved two different insurance companies. One of these companies had refunded the premiums of some complainants but not others. The other company had not refunded premiums to any of the complainants. As of December 1973, the department was arranging for an informal hearing with the latter company and its complainants.

Another insurance company, a Montana company, had a similar record of misrepresentation complaints. From 1970 through 1972, 37 complaints were filed alleging misrepresentation by agents of this company. These complaints were handled by the typical exchange of correspondence. The company claimed it resolved the problem in 1972 by converting a large number of annuities (the policies allegedly misrepresented) to life insurance policies. However, the misrepresentation complaints have continued. Five complaints were received during 1973, with no field investigations being made.

One of the 1973 complainants purchased an annuity at a premium of $100 per month. He claimed the agent told him he would double his money in one year. Two years later the complainant advised the company he could no longer afford the policy and the company converted it to a different policy with a $75 per month premium. Later, the complainant retired and asked to withdraw his money. He stated he had invested over $3,000 by then. The company calculated his policy's cash value as $575. The man

complained to the department, which transmitted the usual correspondence. The company responded that it had discussed the policy benefits with the complainant and he had decided to take no action until the next premium came due. The department sent the complainant a letter stating, "It appears the matter has been satisfactorily resolved." The department did not investigate the alleged misrepresentation further. The complainant informed us the company's agent advised him to hold the policy for another year and he would be able to get his money back.

After the department's transmittal of the usual correspondence, another of the 1973 complainants advised the company he was going to take his loss. He stated he did "not wish to throw good money after bad" and said he believed "doing business with a Montana company was a very poor risk." The department did not investigate the alleged misrepresentation further.

Another man who purchased an annuity from this company advised us he lost more than $500 but did not complain to the department. He said the loss was "just one of life's lessons."

The policyholders' service section supervisor said the department is not a court of law, and therefore, cannot determine whether the agents had, in fact, misrepresented insurance policies. He said that determining whether the policies were misrepresented would boil down to the agent's word that he did not misrepresent the policies against the complainant's word that the policies were misrepresented. He said such a determination would have to be made in a court of law.

Section 40-3503, R.C.M. 1947, prohibits misrepresentation of insurance policies. Section 40-2704 requires the department to employ a field investigator whose primary duty shall be investigations of violations or claimed violations of insurance laws. The department is empowered to hold hearings (Section 40-2720) and to compel testimony at such hearings

(Section 40-2719). Section 40-2724 states the commissioner shall sit in a quasi-judicial capacity during hearings and various sections authorize the department to revoke agents' licenses, suspend or revoke insurers' certificates of authority, revoke the approval of insurance forms, and take other enforcement actions.

The department should use these powers when necessary to protect the public.

In 1971, the Montana Administrative Procedure Act was passed. This act provides that most executive branch agencies authorized by law to make rules and determine contested cases shall adopt rules of practice consistent with the law and submit them to the Secretary of State for implementation in the Montana Administrative Code. The State Auditor's Office has not yet complied with this requirement and, as a result, no such rules exist for the insurance regulatory function. Compliance with this requirement would provide a common basis upon which all affected parties involved with insurance complaints (insurance-buying public, insurance companies and their agents, and the department's staff) might proceed to equitably resolve complaints.

RECOMMENDATION

We recommend that the department:

1. *Employ a field investigator with the necessary ability to investigate insurance complaints.*
2. *Make thorough investigations of insurance complaints where the circumstances warrant such investigation.*
3. *Exercise its powers to hold hearings when the nature of complaints indicate such hearings would be useful.*

4. *Revoke the licenses of agents or companies in those instances where the evidence indicates they have violated the Montana insurance statutes.*

5. *Adopt rules of practice for the insurance regulatory function and file the rules with the Secretary of State pursuant to the Montana Administrative Procedure Act.*

Analysis of Complaints

The complaint supervisor said the monthly list of complaints is alphabetized by insurance company so that they will know how many complaints are coming in against each company. However, no analysis of complaints by insurance companies had been made and no action had been taken against any companies.

The number of insurance complaints has been increasing steadily over the years. The following table shows the number of complaints received during the past several years and the number of complaints per million dollars of insurance premiums collected in the state.

Year	Number of Insurance Complaints	Number of Insurance Complaints Per Million Dollars of Premiums Collected
1972	1,165	5.4
1971	1,173	5.6
1970	989	5.4
1969	854	4.6
1968	750	4.5
1967	731	4.7
1966	743	5.1
1965	859	6.3
1964	820	6.4

The policyholders' service section supervisor was aware that the number of complaints had been increasing each year but had not analyzed any of the data available to determine the cause for the increase of complaints. For example, he did not know whether the increasing number of complaints was due to increased insurance sales, an increasing tendency on consumers to complain, improper action by insurance agents, consumers' difficulty in understanding insurance forms, new types of coverage provided, or other reasons. No specific action had been taken to decrease the number of complaints.

The number of complaints involving each insurance company varies widely with the company. During 1972, one company had .6 complaints per million dollars of insurance premiums collected, and another company had 32.6. The supervisor was aware that some companies had more complaints than others, but had not analyzed the situation and said he did not know why some insurance companies have high complaint rates and others have low rates. For example, he had not analyzed complaints of any company to determine whether the company employed agents who frequently misrepresented their policies, whether the company used forms that were misleading or difficult to understand, or whether there were other causes for its high complaint ratio.

While the number of complaints has been increasing, the percentage of complaints recorded as being resolved in favor of the complainants has been decreasing. The following schedule shows the percentage of complaints recorded as being resolved in favor of complainants each year.

Year	No. of Complaints Received	No. of Complaints Resolved	No. of Complaints Resolved in Favor of Complainant	Percentage of Complaints Resolved In Favor of Complainant
1972	1,165	1,163	734	63.1
1971	1,173	1,087	741	68.2
1970	989	989	797	80.6
1969	854	840	694	82.6
1968	750	735	606	82.4
1967	731	701	556	79.3
1966	743	697	558	80.1
1965	859	859	616	71.7
1964	820	820	560	68.3

The supervisor said he was unaware that the number of complaints resolved in favor of complainants was decreasing and was unaware of the reasons for this decrease. No analysis had been made.

During 1972, about 50 percent of insurance complaints received involved accident and health insurance. The insurance complaints received per million dollars of insurance premiums collected were higher for health insurance than for any other type of insurance. The following schedule shows the complaints per million dollars of insurance premiums by type of insurance.

	Complaints Per Million Dollars of Premiums Collected		
Year	Property and Casualty Insurance	Life Insurance and Annuities	Accident and Health Insurance
1972	4.5	2.0	12.2
1971	4.0	3.1	11.8
1970	4.2	2.2	12.9
1969	3.4	1.3	12.4
1968	3.6	1.8	11.9
1967	3.7	1.4	12.8
1966	4.3	1.2	13.9
1965	5.6	1.6	17.6
1964	5.2	1.4	18.0

The supervisor expressed an unawareness of the relationship between type of insurance and number of complaints received. He had not made any analysis of this type and said he did not know the cause or causes for the high incidence of accident and health insurance complaints.

During the first six months of 1973, 276 complaints were processed by the supervisor, and 214 and 151 complaints were processed respectively by each of the two insurance investigators. Sixty-eight percent of complaints handled by one investigator were resolved in favor of the complainant and 58 percent of complaints handled by the other investigator were resolved in favor of the complainant. The complaint supervisor had not analyzed the trend in the handling of complaints, and said he did not know the workload distribution or of the relationship between complaints handled by one investigator and complaints resolved in favor of the applicant. He said he did not know whether differences in the percentage of complaints resolved in favor of the complainants were due to the types of complaints handled by each investigator or were due to different approaches being used by the investigators.

The insurance complaint files and the complaint records kept by the policyholders' service section contain a wealth of information regarding insurance practices in the state. Proper analysis of this information could disclose trends on the operations of agents, the operation of insurance companies, problems with certain insurance forms, problems with certain types of insurance, misleading advertising, and other problems.

RECOMMENDATION

We recommend that the department:

1. *Develop and implement a program of continuous analysis of insurance complaint data.*

2. *Assign the policyholders' service section supervisor more time to manage the investigation of insurance complaints and determine what type of data could be obtained from analysis of insurance complaint information.*

3. *Use information obtained by analysis of insurance complaints to institute corrective measures.*

Intra-Office Communication on Complaints

There is no formal system of communication between the policyholders' service section and other sections, such as the licensing section and the forms approval section. The policyholders' service section should communicate complaint trends and the results of insurance investigations to the other sections so they can use the information to more effectively fulfill their functions.

The alleged misrepresentations of insurance policies discussed on pages 96-99 provide an example of the need for such communication. As previously discussed, the policyholders' service section began receiving complaints alleging misrepresentation by one agent and his staff as early as April 1971. The policyholders' service section did not advise the licensing section of the alleged misrepresentation by these agents. The complaint supervisor said he believed it was unnecessary to inform the licensing section of the complaints since the individuals involved were already licensed. On February 28, 1972, the company involved requested clearance for the agents because they were applying for licenses in Idaho, Washington, Oregon, and Nevada. On March 2 and 3, 1972, the licensing section advised each of these states there were no complaints against the agents whereas, if the licensing supervisor had known the complaints

existed, he could have requested they be verified before notifying the other states.

Although the first misrepresentation complaints were received in 1971, the bulk of complaints were received after the department's March 1972 letters.

The agents were licensed as non-residents in Oregon in May 1972. As a result of subsequent events, in September 1972, the department advised Oregon officials there were numerous complaints against the agents. Department officials stated they could not issue a clearance when there was information to the contrary. In November 1972, the department sent another letter to Oregon advising that Montana law and existing circumstances would not preclude the agents from being licensed in Montana. The agents were then shortly licensed as residents in Oregon. We didn't determine whether the agents were licensed in Idaho, Washington, or Nevada.

As this example illustrates, the insurance complaints contain a great deal of information that should be communicated to other sections in the department.

RECOMMENDATION

We recommend that the department establish systematic procedures for the policyholders' service section to inform other sections of insurance complaints involving agents, forms, insurance rates, or other matters that are normally handled by such sections.

FINAL COMMENTS

We have reviewed the comments and recommendations contained in this report with the State Auditor. The cooperation and assistance provided to us by him and his staff are sincerely appreciated.

Respectfully submitted,

Morris L. Brusett
Legislative Auditor

February 15, 1974

AGENCY REPLY

STATE OF MONTANA

OFFICE OF

E. V. "SONNY" OMHOLT

STATE AUDITOR

COMMISSIONER OF INSURANCE
INVESTMENT COMMISSIONER
CENTRAL PAYROLL SYSTEM

HELENA, MONTANA 59601

MR. CHAIRMAN AND MEMBERS OF THE LEGISLATIVE AUDIT COMMITTEE:

I wish to thank the Chairman and members of this Committee for this opportunity to offer my comments.

I have been placed in my position by the people of the State of Montana to serve them as State Auditor and Ex Officio Commissioner of Insurance. It is a well known fact that I have always placed the greatest emphasis on consumer protection. We have departmentalized my office for certain specific functions in regards to the supervision and regulation of insurance.

I would call your attention to the progressive legislation on insurance matters, which we have submitted for the consideration of the Legislative Assemblies, namely, the Montana Insurance Guaranty Association Act for both Property and Casualty and now pending before this Legislature, the Montana Model Life and Health Insurance Guaranty Association Act. Upon passage of this Act - hopefully in this Session - the people of the State of Montana will be protected from any monetary loss caused by any insurance company's insolvency.

I would, also, call to your attention certain Legislative changes, which we submitted to the Legislature and which have been approved that will enhance the General Fund in excess of $300,000 per annum.

The National Association of Insurance Commissioners, of which I am an active member, is promulgating desirable Uniform Legislation, which should be enacted and made into law, but all require additional staffing to carry out the responsibilities of these Acts.

Certain systems to detect problem companies in the areas of insolvency, which we call the "early warning system" are being developed both for Property and Casualty and Life and Health insurers.

A review of the examination system, as it now exists, is being studied.

A Data Bank is being developed, which will give current information on various aspects of insurance.

Uniform complaint handling procedures are being developed on a Nationwide basis.

Uniform agent's licensing and testing procedures are being promulgated.

I want to make the Committee aware that the supervision and regulation of insurance is the last vestige of Interstate Commerce that is still regulated by the various States. The Federal Government is expressing a great deal of interest in the Federal regulation of insurance.

The power to regulate, also, encompasses the power to tax. If

the State of Montana were to lose those monies now generated by premium taxes and fees paid by the insurance industry, this would have great impact upon the State and its political subdivisions, but most of all, the people of Montana, as this industry, my fellow-Montanans, generated in 1973 over 6.8 million from taxes and other fees on insurance.

Thus, we owe the consumer and industry a more equitable return for this vast input of money.

As we know, several well known companies in America today have become successful by advertising the fact that they are second best. Montana is second best, but not from the top of the list, but from the bottom, as we rank 49th in the Nation as to budget allocation for insurance supervision and regulation. This is less than 50% of what other States allocate to budget in comparison to revenue.

We are, and will continue to be, our own greatest critics. As supported by the Legislative Audit, on page 10, it is a well known fact that we are understaffed and underpaid. In my budget requests, I have repeatedly asked for additional personnel and especially, those people of expertise in the business of insurance regulation. In the business of insurance, we are dealing in areas of contracts. This Department has sought the services of a full-time staff attorney and have been repeatedly denied. Also, we have sought the services, contractual or otherwise, of actuaries paid by the State of Montana. Our staff and Department heads are now doing clerical work when they should be devoting their time to

improving systems, which would enhance the regulation and supervision of insurance in Montana.

Do you realize that the Montana Insurance Department regulates more companies than the State of New York?

The Montana Insurance Department will continue to expand its services to the insurance public, the consumer, in direct proportion to our budgetary capabilities, as recognized by the Legislative Audit report,which will be reviewed by your Committee.

In closing, let me state that I will continue to serve the people of Montana by managing an Insurance Department that is well known and respected, not only by the people of Montana, but by other States as well, as I have done in the past and will continue to do in the future - on a bi-partisan level.

STATE OF MONTANA

OFFICE OF

E. V. "SONNY" OMHOLT

STATE AUDITOR

COMMISSIONER OF INSURANCE
INVESTMENT COMMISSIONER
CENTRAL PAYROLL SYSTEM

HELENA, MONTANA 59601

February 14, 1974

Mr. Morris L. Brusett
Legislative Audit Committee
Capitol
Helena, Montana

Report on review of the Insurance Regulation Program

Commentary on recommendations contained therein:

Page 12 - A resume of the Montana Insurance Code and related laws setting forth the scope of the code as it relates to the operations of the insurance department will be prepared and staff members will be so informed.

Page 13 - This will be done.

Page 14 - This is being done.

Page 18 - These are excellent recommendations and will be complied with.

Page 20 - We have no objection to this recommendation, which would require legislative clarification of the present law.

Page 22 - The systems approach is good. This will be done within the realm of practicability.

Page 23 - This will be done, subject to additional staffing.

Page 25 - This is acceptable. The problem is evaluating management.

Page 27 - This is acceptable. However, the basic issue is to weigh the due process of applicant approval against the practical problems of predicating the consumer buying public.

Page 29 - This is being done. We hold the company responsible for the acts of its agents.

Page 30 - This will be done - subject to adequate staffing.

Page 31 - This will be done - subject to adequate staffing.

Page 32 - This will be done.

Page 33 - Gray area. Legislative measure would be required. Considerable question as to the applicability of the term "trip" to other forms of insurance issued in conjunction with trips.

Page 36 - This will be done - additional staffing required.

This will be done - additional staffing required.

Page 37 - O. K. This would require legislation.

Page 39 - We concur that this would be desirable. Additional staffing would be necessary.

Page 40 - No objection to this recommendation. Additional personnel would be required.

Page 41 - We concur with this suggestion. Additional personnel would be necessary.

Page 43 - This is in the process.

Page 44 - This is in the process.

Page 45 - This is in the process.

Page 47 - This is being taken into consideration in the drafting of the new agents examinations and will be complied with.

Page 48 - This will be complied with.

Page 50 - This will be complied with.

Page 54 - 1. Such a practice is not condoned by the department and if such alterations have been made it was without the knowledge or consent of the Commissioner.

2, 3 and 4. All of these situations have been corrected.

Page 59 - This will be done.

Page 61 - A survey of applicants has been instituted. Examinations at other points, if found to be viable, would be subject to budget resources.

Page 61 - Good suggestion with additional staff this could be accomplished.

All title and farm mutual insurers have been put on notice of this requirement as of this date, even though the "grandfather" clause of our codes may apply in some instances.

Page [illegible] - This will be done.

Page 65 - This would be a legislative matter.

Page 69 - No objection. Subject to budget appropriation.

Page 70 - No objection.

Page 72 - This recommendation is acceptable. The NAIC Data Bank has now been [illegible] which would provide some of the information.

This is acceptable.

Page 75 - We are in the process of inventorying safe deposit boxes and an up-to-date system of accounting will be implemented.

Page 76 - No objection. Our records are being up dated.

Page 77 - This should be established by law.

Pages 79 - 80 - We concur with the recommendations.

Page 82 - This is tax reform. Should be referred to the Department of Revenue.

Page 84 - This is a tax reform measure and should be referred to the Department of Revenue. If implemented would require additional staffing.

Page 86 - This is being done.

Page 90 - We agree. Our immediate problem is that we are understaffed in this area also.

Page 93 - We concur with this recommendation. We have been working with the people involved over the past three years to effect these desirable changes.

Page 95 - We are in the process of implementing the NAIC model procedures in complaint handling.

Pages 99 - 100 - We fully agree that the recommendations would be desirable and helpful. However, it would be necessary to have a field investigator and a full time "in-department" attorney to implement these changes.

We are presently operating in this regard within budget limitations.

Pages 103 - 104 - 1. This will be done. Up-dating now in progress.
2. See recommendation on page 95. NAIC model uniform complaint handing procedures being adopted.
3. We agree this would be helpful and will be developed.

Page 105 - This is being adopted by present personnel changes within the department and will be utilized on a scheduled basis.

E. V. "SONNY" OMHOLT
State Auditor & Ex Officio
Commissioner of Insurance

EVO:eh